No. 151

IN THE

Supreme Court of the United States

October Term, 1939

PEARL E. DEPUTY and the SUSSEX TRUST CO., a Corporation of the State of Delaware, as Administratrix and Administrator of the Estate of Willard F. Deputy, Deceased, Late Collector of Internal Revenue, *Petitioner.*

v.

PIERRE S. DU PONT

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

BRIEF FOR RESPONDENT IN OPPOSITION

GEORGE WHARTON PEPPER,
JAMES S. Y. IVINS,
Attorneys for Respondent.

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INDEX.

CASES CITED.

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Opinions Below

The opinion of the District Court (R. 222-243) is reported in 22 F. Supp. 589. The opinions of the Circuit Court of Appeals (R. 264-268) are reported in 103 F. (2d) 257.

Jurisdiction

The judgment of the Circuit Court of Appeals was entered March 28, 1939 (R. 268) and the petition for certiorari was filed June 28, 1939. Petitioner invoked the jurisdiction of this Court under section 240(a) of the Judicial Code (U. S. Code, Tit. 28, § 347).

Question Presented

Whether the carrying charges paid by respondent for the forbearance of a loan of borrowed stock were, in the circumstances, deductible from gross income in computing taxable net income as

(a) ordinary and necessary business expenses, or
(b) interest upon indebtedness.

Statute Involved

Revenue Act of 1928:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) *Expenses.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *.

(b) All interest paid or accrued within the taxable year on indebtedness, * * *.

SEC. 24. ITEMS NOT DEDUCTIBLE.

(a) *General rule.*—In computing net income no deduction shall in any case be allowed in respect of—

(1) Personal, living, or family expenses;

* * * * * * *

Statement

The statement of facts in the petition (p. 3) is sufficient to reflect the nature of the issues. The respondent contended before the Circuit Court of Appeals that the carrying charges on the borrowed stock were deductible from gross

income either as ordinary and necessary business expenses, or as interest on indebtedness. The Circuit Court of Appeals found it necessary to pass on only the first of these contentions, in which it upheld respondent's position. Should a writ of certiorari be allowed both questions will be before this Court.

Argument in Opposition to Granting of the Writ

Four reasons are advanced in support of the application for certiorari: First, that the decision of the Circuit Court of Appeals is in conflict with the decisions of this Court and with certain decisions of the Circuit Courts of Appeals; second, that the decision sought to be reviewed was erroneous because of too narrow an approach to the question involved; third, that the decision was also erroneous because based upon the assumption (alleged to be unfounded) that "conserving and enhancing one's estate constitutes the carrying on of a trade or business"; and, finally, that the decision below is in conflict with a certain decision of the Circuit Court of Appeals for the Second Circuit, to wit, *Terbell* v. *Commissioner*, 71 F. (2d) 1017 (1934).

It is respectfully submitted that none of the reasons thus advanced will stand careful analysis and that none of them is sufficient to require the exercise of supervisory jurisdiction by this Court.

I

The contention that the decision of the Circuit Court of Appeals is in conflict with authority will be found on analysis to be based upon the assumed validity of petitioner's second reason. It is nothing more than an assertion by the petitioner that if his interpretation of the facts and law in his second reason were accepted, it would then follow that the decision was in conflict with the authorities cited under his first reason. The converse of this proposition is likewise true: namely, that if the second reason is fallacious, the alleged conflict with authority disappears. Therefore it is upon the second reason that attention must be focused.

II

The consideration of the second reason requires (for the moment) the assumption that respondent was in fact engaged in the business which the District Court made the subject of its thirty-seventh finding of fact as follows: "The plaintiff's business was primarily that of conserving and enhancing his estate." It was upon the basis of this finding of fact that the Circuit Court of Appeals reached the conclusion which is now criticized.

We cannot do better than quote from the concurring opinion of Judge Maris, as follows:

> "Section 23 of the Revenue Act of 1928 provides that in computing net income for income tax purposes there shall be allowed as deductions 'all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.' The District Court found as a fact in this case that 'the plaintiff's business was primarily that of conserving and enhancing his estate.' The finding was undoubtedly supported by ample evidence. If we premise this fact, as I think we must, it follows that the plaintiff was entitled, in computing his taxable net income for the year 1931, to deduct all the ordinary expenses paid during that year which were necessary to conserve his estate.
>
> "At the beginning of the year the plaintiff was faced with the fact that he owed the Delaware Realty and Investment Company 141,912 shares of common stock of E. I. du Pont de Nemours & Company. The history of this loan and the purposes for which the stock was borrowed are in my view wholly irrelevant. Whatever the reason, the fact remained that in 1931 he found himself under a binding obligation to the Delaware Company either to return the borrowed stock or to pay an amount equivalent to the dividends on the borrowed shares plus the taxes paid by the Delaware Company by reason of the loan. Since he no longer owned the shares borrowed the return of them would have necessarily involved the depletion of his estate by the amount required to purchase an equivalent number. He elected

to take the only other course which was open to him and paid to the Delaware Company the sum of $647,711.56, which represented the amount of the dividends paid on the stock plus the taxes of the Delaware Company with respect thereto.

"This payment unquestionably conserved the plaintiff's estate. If it had not been made his invested funds would have faced the certainty of a serious diminution. The necessity of the expense is clear. The diminution of his principal which would have resulted if the payment had not been made would undoubtedly have carried with it an inevitable diminution in taxable income which might well have been substantially equivalent to the deduction here sought. The inherent justice of his claim will thus be seen."

The facts in the case are peculiar; it would be difficult to generalize from the decision thus made or to apply it as a controlling authority to more usual states of fact. The stock-loan which the respondent decided to repay by borrowing the necessary shares from another lender was a loan which had been standing for ten years and serviced by the respondent during all that time. It is a debatable question whether the original borrowing was a step taken in the ordinary course of respondent's business. To the consideration of that debatable question the District Court had given primary attention. For the reasons given by Judge Maris the decision of that debatable question was unnecessary and the complicated facts out of which it arose were irrelevant to the present controversy. It is respectfully suggested that upon this particular record the decision of the Circuit Court of Appeals was sound and that there is nothing in the second reason advanced by the petitioner that requires that it be disturbed. There was an additional reason upon which (had the first point been decided differently) the conclusion reached by the Circuit Court of Appeals might have been based. The price exacted by the lender of the borrowed stock was a certain annual payment of sums equal to dividends and taxes. This, it was con-

tended by the respondent, was a payment of "interest" within the meaning of the Revenue Act. Upon this point the observation of Judge Maris was as follows:

> "I am equally satisfied that the expense was an ordinary one within the meaning of the statute. Certainly there is no expense in human experience which is more ordinary than that incurred by a debtor in fulfilling his agreement with his creditors. It is true that this expense usually takes the form of interest. It may well be that the expenditure which the plaintiff made in this case was a payment of interest in the broadest sense. It is certain, however, that it was compensation for the loan of stock which he had made and as such it was an ordinary and usual expense of a transaction of that character."

The District Court had ruled that the carrying charges on the borrowed stock were not deductible as interest, on the theory that "interest" as used in federal taxing statutes means compensation for the use, forbearance or detention of money (R. 241). The only place where we have been able to find a Congressional definition of "interest" is in the Code of the District of Columbia, Title 17, Chap. 1. A reference to the first section of that chapter shows the comprehensive meaning given by Congress to the term "interest."

> "The rate of interest in the District upon the loan or forbearance of any money, goods, or things in action, and the rate to be allowed in judgments and decrees, in the absence of express contract as to such rate of interest, shall be six dollars upon one hundred dollars for one year, etc."

Petitioner emphasizes the refusal of the Appellate Court to consider the *motive* of the first loan. When, however, the entire history is taken into consideration there is one significant fact that stands out in bold relief. It is this: that

simultaneously with the first borrowing of stock in 1919 and (according to petitioner's theory) as part of the same transaction, respondent sold the borrowed stock for $2,880,000. This means that during the life of the loan, down to and including 1931, he had the use of that large sum. In actual and practical effect therefore payments of the carrying charges on the loan were the price paid by the borrower for the use of the money. In view of all the foregoing considerations it is respectfully submitted that neither the second reason nor the first (which is based upon it) affords any justification for the grant of certiorari.

III

As if conscious of the insufficiency of the prior reasons, the petitioner boldly asserts it to be error to assume that "conserving and enhancing one's estate" constitutes the carrying on of a trade or business within the meaning of section 23(a) of the applicable Revenue Act. In order that the third reason advanced may support his contention the petitioner must go so far as to assert that there really is no such business. A narrower contention than this would not be serviceable to the petitioner because if, on any state of facts, such a business can exist, then it must be taken as a fact that it existed in the instant case because the trial court so found and there was unquestionably evidence to support the finding.

It is respectfully submitted that on both reason and authority the conservation and enhancement of a great estate is assuredly a *business* within the meaning of the Act of Congress.

On principle, a citizen so engaged is a producer of taxable wealth. His business is lawfully to increase his income and therefore to produce or create a larger estate. The larger the net estate, the greater his success in his business. His net estate is the excess of his assets over his

liabilities. If he allows his liabilities to increase faster than his assets he is on the way to bankruptcy. To deal with liabilities in an intelligent way is just as much a part of his business as to make advantageous sales and purchases of assets or to take intelligent steps to enhance the value of the assets which he retains. The interest of the federal government coincides with his own: to the extent that the business yields a larger income, a greater income tax is paid; and to the extent that the net estate is increased, the estate tax at death will be proportionately greater.

The authorities (without exception so far as the respondent can find) are unanimous in the recognition of such an activity as a business within the Act of Congress. There are of course cases in which the facts do not justify a finding that the taxpayer in those cases was actually so engaged. The question, however, is primarily one of fact and has been consistently so treated.

Reliance is placed by the petitioner on *Kane* v. *Commissioner*, 100 F. (2d) 382 (C. C. A. 2d); 1938. "While we do not say," said the Court in that case, "that the taxpayer might not carry on a business through an agent, it was not shown here that enough was done by the taxpayer or her agents to constitute the carrying on of a business." In other words, the question was one of degree and the Court merely held that upon the facts of the *Kane* case the so-called business was non-existent. A reading of the opinion in the *Kane* case is sufficient to show how remote the situation disclosed by the record in the instant case is from the petty transactions which were under consideration in the *Kane* case.

Reliance is also placed by the petitioner upon the decision of this Court in *Van Wart* v. *Commissioner*, 295 U. S. 112 (1935). The relevancy of this citation is difficult to understand. It was a case of guardian and ward. It was found as a fact that the ward was not engaged in any business and that, so far as appeared, the same thing was true of

the guardian. The guardian's contention was that an attorney's fee was deductible as a necessary business expense, although there was no business in connection with which the service could have been rendered. To state the case is to distinguish it. The same thing may fairly be said of the one remaining authority cited in the petition, *Monell* v. *Helvering*, 70 F. (2d) 631 (C. C. A. 2d); 1934. In that case the sole beneficiary of an estate agreed to pay an amount equalling one-half of estate tax refunds to be procured by the attorney's activity. The decision was merely that such part of the fee as was attributable to interest on refunds was to be regarded as a payment made to enforce the beneficiary's personal rights and was not deductible from income as an ordinary and necessary expense in carrying on a trade or business. As if in recognition of the fact that the three cases relied upon have been overstrained in an attempt to make them applicable to the instant case, a footnote has been printed at the bottom of page 14 of the petition in which it is conceded that "Other decisions have indicated that investment activity may constitute a business, if it is sufficiently extensive and regular."

Two cases are cited by the petitioner in this connection, one *Kales* v. *Commissioner*, 101 F. (2d) 35 (C. C. A. 6th); 1939, and the other, *Miller* v. *Commissioner*, 102 F. (2d) 476 (C. C. A. 9th); 1939. In the former there is a careful opinion by Judge Simons, which reviews all the authorities and reaches the conclusion that the activities of the taxpayer upon the facts of that case were such as to "bring her deductions within the permissible scope of the statute." In the latter, there is similarly a careful opinion by Judge Stephens, who thus states the conclusion of the court: "We think the present case is unlike the *Kales* case, supra, and in no substantial manner to be distinguished from the *Kane* case, supra." In both cases the Court clearly recognized that the question of the existence or non-existence of a business was to be determined by the facts in each particular case. In the one it was found that such a business ex-

isted; in the other, on the contrary, it was held that the business was non-existent.

When the authorities are reviewed it is impossible to escape the conclusion that there *is* such a thing as the business of conserving and enhancing an estate within the meaning of the Act of Congress; that the only differences between the decided cases have to do with the facts alleged to be sufficient to constitute a doing of such business and that when, as here, the fact of business has been found by the trial court, the finding should not be disturbed on appeal if the evidence before the Court was sufficient to justify, if not to require, the finding.

IV

The fourth and last reason advanced by the petitioner is an alleged conflict between the decision of the Circuit Court of Appeals for the Third Circuit in the instant case and the decision by the Circuit Court of Appeals for the Second Circuit in *Terbell* v. *Commissioner*, 71 F. (2d) 1017; 1934. This contention relates exclusively to the original borrowing of stock by the respondent, the details of which were on the peculiar facts of the instant case regarded as irrelevant by the Circuit Court of Appeals. The petitioner's theory is that *if* the Court ought to have considered the nature of the original borrowing and that if (having so considered it) the Court had decided that the borrowing was part of a transaction involving a "short sale" the decision would have been in conflict with the *Terbell* case. It has already been urged in this brief that the Circuit Court of Appeals in the instant case was right in disregarding the nature of the original loan. If, however, the Court had considered it and had decided that the borrowing was a transaction in line with respondent's business, there would have been no resulting conflict with the decision in the *Terbell* case. That was an appeal from the United States Board of Tax Appeals. The Board was affirmed in a per curiam opinion, which reads thus:

"Affirmed on the authority of Bonwit, Teller & Co. v. Commissioner, (C. C. A.) 53 F. (2d) 381, 82 A. L. R. 325; Bedell v. Commissioner, (C. C. A.) 30 F. (2d) 622, and Central Bank Block Ass'n v. Commissioner, 57 F. (2d) 5 (C. C. A. 5)."

The record before the court in that case presented several questions for decision. When reference is had to the authorities upon which the affirmance was expressly based, it will be found that no one of them deals with the question now under consideration, but with features of the *Terbell* case not present in this one. In the *Bonwit Teller* case the decision was merely that a petitioning taxpayer had failed to discharge the burden of establishing that a brokerage fee paid for negotiating a lease of realty was a deductible expense. In the *Bedell* case the question was whether a taxpayer engaged in the real estate business could deduct as an expense of that business losses sustained by him in connection with the purchase and sale of negotiable securities, which had no relation whatever to the business in which he was in fact engaged. Of course the decision disallowed the deduction. The third and last case underlying the *Terbell* decision (i. e., the *Central Bank* case) was concerned exclusively with the question how much of a single commission paid for negotiating a long-term lease could be deducted as an expense in any one year of the term.

The sound conclusion to reach with respect to the petitioner's fourth reason is that the *Terbell* decision was based upon elements that are absent in the instant case, each one of which had been authoritatively and soundly disposed of in the earlier decisions on which the Circuit Court expressly relied. The Court did not decide against the deductibility of amounts paid to service a loan of stock which had been borrowed to cover a short sale. On the other hand, this was precisely the point which was decided by the Circuit Court of Appeals for the Fourth Circuit in *Dart* v. *Commissioner*, 74 F. (2d) 845 (1935) and it was there decided in favor of

the deductibility of the payments in question. This was the case which was cited with approval by Judge Maris in the course of his concurring opinion. If the instant case could be thought of as inconsistent with the *Terbell* decision, then the *Dart* case would have been likewise inconsistent with it;[1] but in the *Dart* case the Commissioner did not seek certiorari—presumably because the decision was by him believed to be unassailable.

On the whole, therefore, it is respectfully submitted that no one of the reasons advanced by the petitioner is really sound and that there is no occasion for the review by this Court of the decision of the Circuit Court of Appeals.

GEORGE WHARTON PEPPER,
JAMES S. Y. IVINS,
Attorneys for Respondent.

August 3, 1939.

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[1] In petitioner's last brief below ["Answer of Appellee to Reply Brief"] he *relied* on the distinction between the *Terbell* and *Dart* cases, showing that in the former there was no evidence that the taxpayer was in business, while in the latter the taxpayer was in the business of buying and selling stocks. No suggestion was made that the *Dart* case was erroneously decided.

BRIEF FOR THE RESPONDENT

IN THE

Supreme Court of the United States

October Term, 1939.

No. 151.

PEARL E. DEPUTY and the SUSSEX TRUST CO., a Corporation of the State of Delaware, as Administratrix and Administrator of the Estate of Willard F. Deputy, Deceased, Late Collector of Internal Revenue,

Petitioner,

v.

PIERRE S. du PONT.

BRIEF FOR RESPONDENT.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

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INDEX.

APPENDICES.

CASES.

(Page numbers followed by "a" are in Appendix.)

CASES—Continued.

CASES—Continued.

CASES—Continued.

OTHER AUTHORITIES.

Statutes.

Economists.

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v.

PIERRE S. DU PONT.

BRIEF FOR RESPONDENT.

I.

RESPONDENT'S STATEMENT OF THE QUESTIONS INVOLVED.

A taxpayer, whose business is that of conserving and enhancing his estate, is indebted to A, a corporate lender, for shares of stock in the X company, borrowed two years previously. The taxpayer, at the time of borrowing the shares, agreed to pay to A, annually, sums equal to dividends declared by X on the borrowed shares and also sums sufficient to indemnify A against any additional tax assessed against A because of the transaction. The sums so received by A are taxable as a part of A's income. Must they also be included in the taxable income of the payor, or may he deduct such sums paid to A from his gross income in the year in which he, in fact, paid them, either as part of the "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business" or as "interest paid on indebtedness?"

II.

CONCISE ABSTRACT OF THE FACTS.

Under a contract made in 1919, the respondent du Pont borrowed, with a ten-year maturity, 9,000 shares of stock of the du Pont Company from a concern styled the Christiana Company. As the ten-year period, dating from December 23, 1919, drew to a close, the respondent, on October 25, 1929, entered into an agreement with another corporation, styled Delaware Realty & Investment Company, whereby that Company undertook to lend him the number of shares of the du Pont Company required by him to repay the Christiana loan.

The terms of the respondent's contract with the Delaware Realty Company provided that he would return the du Pont Company stock borrowed from it in kind within ten years after October 25, 1929, would pay to it an amount equivalent to all dividends declared by the du Pont Company upon the shares borrowed, and would reimburse the Delaware Realty Company for all taxes paid by it by reason of the receipt by it from the respondent of the sums equivalent to the dividends declared upon the stock borrowed. In 1931, the taxable year in question, respondent paid to the Delaware Realty Company the sum of $567,648., being the amount equivalent to the dividends paid by the du Pont Company upon the shares for which he was then indebted. In addition thereto the respondent paid to the Delaware Realty Company the sum of $80,063.56, which was, in fact, the amount of federal income tax imposed upon the Delaware Realty Company by reason of the payments equivalent to the sum of declared dividends which it had received from the respondent. The total of these two items, $647,711.56, is the amount of the deduction to

which the respondent claims he is entitled in the suit at bar. If this deduction is allowed, the respondent will be entitled to an affirmance of the judgment in his favor of $172,351.64, in accordance with the opinion of the Circuit Court of Appeals.

The foregoing summary statement presents all the facts which the Circuit Court of Appeals deemed relevant. If, however, this Court wishes to explore the transaction occurring in 1919 when du Pont originally borrowed stock from the Christiana Company, the following additional statement will be in order.

In December 1919 du Pont was the beneficial owner of 95,139 shares of the stock of the du Pont Company (R. 142, 143). While he was an executive officer of that corporation, his business was primarily that of conserving and enhancing his estate (R. 221, 152-156). The du Pont Company, following the World War, was planning to develop its peace-time manufacturing line and was desirous of tying into its organization through stock ownership nine capable young executives (R. 131-136). After much discussion it was decided by the Company to enable each of the nine to buy 1000 shares of its stock by lending him the purchase price, taking the shares as collateral and applying future dividends in reduction of the loan (R. 148, Ex. K of Stip.). As the 9000 shares required were not otherwise available, respondent agreed to sell 1000 shares to each of the nine at a price determined by a fair appraisement. Respondent had recently put 24,000 of his shares into two short-term trusts (R. 143, Exs. N, O, P of Stip. R. 75-85). from which he might have reclaimed the 9000 shares by paying to the trustees approximately a fourth of the pur-

chase price receivable from the executors. Instead of doing this, however, he decided to borrow the shares needed to perform his contract with the nine and apply the purchase money to other uses. The Christiana Company, of which du Pont was a large shareholder, was a heavy owner of du Pont shares and agreed to lend him what he needed (R. 48, 49, Ex. D. of Stip.). This loan, thus made to cover a short sale, was to run for ten years, the borrower agreeing to pay to the lender in each year a sum equal to the dividend which Christiana would have received had the loan not been made (R. 48, 49, Ex. D. of Stip.). The transaction was carried through as planned, the sale to the nine was consummated at $320. per share and the purchase money duly paid to du Pont in cash (R. 16, 17). In making this sale du Pont by borrowing the necessary shares was able to realize $2,880,000. in cash for immediate use in his business. This he proceeded to turn over through transactions in General Motors stock which ultimately yielded him a great profit. (See record of Board of Tax Appeals in *du Pont v. Commissioner*, 37 B. T. A. 1198, cited on page 30 of petitioner's brief.) In 1921, however, the du Pont stock declined in value from $320. to $156. The nine executives were thus caught with a heavy outstanding obligation secured only by greatly impaired collateral. Du Pont came to their relief and turned over to each executive 400 shares of Christiana stock which at that time was worth $400 a share, to be used as additional collateral, he reserving to himself an option to repurchase which in fact he never exercised. Thereafter all went well. Successive stock dividends declared by the du Pont Company, together with reductions in the par value of its shares, operated to increase the number of shares which respondent was bound

to pay to Christiana. Each year he made the cash payments called for by the contract of loan. When in 1929 the ten-year period was about to expire the number of shares due Christiana had increased to 142,212. Not having at the time sufficient shares at his disposal he borrowed from the Delaware Realty and Investment Company the number which he needed and with them discharged his pre-existing debt. Thereafter the course of events was as set forth in the earlier part of this statement.

III.

ARGUMENT.

No essential facts are in dispute. The sole purpose of this brief, therefore, is to convince this Court that the judgment below was sound as a matter of law and therefore should not be disturbed.

The reasons supporting this contention may be summarized as follows:

1. There *is* such a "trade or business" (to quote the language of the applicable statute) as the conservation and enhancement of a taxpayer's estate; and the respondent in this case was in fact busily and successfully engaged in it.

2. The decision to discharge a preexisting loan of stock by borrowing rather than by buying was a mere exercise of judgment in the course of the respondent's business; and the cost of "servicing" the new loan was an ordinary and necessary expense of that business.

3. The expenditure necessary to carry the new loan was the price of the lender's forbearance; and the payment of this price was in its nature "interest on indebtedness" notwithstanding that the subject-matter of the indebtedness was stock and not money.

4. Since the claimed deductions are only carrying charges and not the principal of the loan, it should seem that the nature of the original debt which was discharged by the loan is really unimportant; but if and when it is scrutinized, it will be found to have been in fact a debt incurred to conserve and enhance the respondent's estate.

The applicable provisions of the Revenue Act of 1928 (which was in force during the tax year here in question) are as follows:

"Sec. 23. Deductions From Gross Income.

"In computing net income, there shall be allowed as deductions:

"(a) Expenses.—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable allowance for salaries or other compensation for personal services actually rendered; traveling expenses (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken, or is not taking, title or in which he has no equity.

"(b) Interest.—All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued to purchase or carry obligations or securities (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation under this title."

With these statutory provisions in mind, the Court is respectfully requested to consider seriatim our reasons for asserting that the judgment below should not be disturbed.

1. The activity of a taxpayer in conserving and enhancing his estate under such circumstances as this record discloses is a "business" within the broad language of the Act of Congress and has long been so recognized in administrative practice and by judicial decision.

As far as *facts* are concerned, this proposition is based on the following findings by the District Court:

"37. The plaintiff's business was primarily that of conserving and enhancing his estate."

Finding No. 36 is, in part, as follows:

"In 1919, the plaintiff maintained an office in Wilmington, Delaware, for the conduct of his business affairs. He had seven or eight employes in his office at that time. In 1920, he established an additional office in New York for the conduct of his business. He has maintained both such offices ever since such years. The expense of maintaining such office was $36,310.67 in 1931. In 1931, plaintiff sold 63,346 shares of stock in various corporations in which he was a stockholder."

Upon this point Judge Maris, in his concurring opinion, had this to say:

"Section 23 of the Revenue Act of 1928 provides that in computing net income for income tax purposes there shall be allowed as deductions 'all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business.' The District Court found as a fact in this case that 'the plaintiff's business was primarily that of conserving and enhancing his estate.' The finding was undoubtedly supported by ample evidence. If we premise this fact, as I think we must, it follows that the plaintiff was entitled, in computing his taxable net income for the year 1931, to deduct all the ordinary expenses paid during that year which were necessary to conserve his estate."

The case was tried in the District Court and argued in the Circuit Court of Appeals upon the theory that there *is* such a business as conserving and enhancing an estate; and the only question upon this phase of the case argued by counsel or considered by the courts below was whether du Pont was *in fact* engaged in that business. In this Court, for the first time, we are now met with the contention that there is no such business. No decision is cited

by the petitioner which lends color to such a proposition. There are cases which hold that, upon the facts, a particular taxpayer was or was not engaged in the business. All of them are at least impliedly authority that such a business does exist. Indeed, the decisions of the courts and of the Board of Tax Appeals acquiesced in by the Commissioner of Internal Revenue, as well as the rulings of the Treasury Department and the regulations, have consistently for upwards of twenty years recognized that an individual (as well as a corporation) may be engaged in the business of conserving and enhancing his estate. "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially re-enacted statutes, are deemed to have received Congressional approval and have the effect of law": *Helvering v. Winmill*, 305 U. S. 79, 83 (1938). In view of these facts, it is to say the least rather startling to hear such a contention now made for the first time. We shall not labor the point here. A thorough historical treatment of it will be found in Appendix I to this brief at page 1a. This demonstrates, we think, that the contention is wholly without merit.

To regard the conservation and enhancement of an estate as a business is, we submit, altogether reasonable. Just as the owner of a farm is undoubtedly in business when he attempts to secure from his acreage a maximum yield, so the owner of securities is engaged in business if he is not content to collect the income on what he already has but is actively engaged in turning over his holdings in an effort to produce two dollars where one existed before. A citizen so engaged is a producer of taxable wealth. His business is lawfully to increase his income and, therefore, to produce

or create a large net estate. The larger the net estate, the greater his success in his business. Particularly from the point of view of government, this is a fair and reasonable conception. The larger the estate which the business man produces the greater the tax which will be payable to government in respect to it, both during life and at death. The expenses of the business of conserving and enhancing it ought therefore in all fairness to be deductible.

2. The decision to discharge a preexisting loan of stock by borrowing rather than by buying was a mere exercise of judgment in the course of the respondent's business; and the cost of "servicing" the new loan was an ordinary and necessary expense of that business.

Upon this point the observation of Judge Maris was as follows:

> "At the beginning of the year the plaintiff was faced with the fact that he owed the Delaware Realty and Investment Company 141,912 shares of common stock of E. I. du Pont de Nemours & Company. The history of this loan and the purposes for which the stock was borrowed are in my view wholly irrelevant. Whatever the reason, the fact remained that in 1931 he found himself under a binding obligation to the Delaware Company either to return the borrowed stock or to pay an amount equivalent to the dividends on the borrowed shares plus the taxes paid by the Delaware Company by reason of the loan. Since he no longer owned the shares borrowed, the return of them would have necessarily involved the depletion of his estate by the amount required to purchase an equivalent number. He elected to take the only other course which was open to him and paid to the Delaware Company the sum of $647,711.56, which represented the amount of the divi-

dends paid on the stock plus the taxes of the Delaware Company with respect thereto. This payment unquestionably conserved the plaintiff's estate. If it had not been made his invested funds would have faced the certainty of a serious diminution. The necessity of the expense is clear. The diminution of his principal which would have resulted if the payment had not been made would undoubtedly have carried with it an inevitable diminution in taxable income which might well have been substantially equivalent to the deduction here sought. The inherent justice of his claim will thus be seen. I am equally satisfied that the expense was an ordinary one within the meaning of the statute. Certainly there is no expense in human experience which is more ordinary than that incurred by a debtor in fulfilling his agreement with his creditors."

The expenses incident to the enhancement of an estate may be described as asset-expenses. Those incident to conserving the estate from loss may be conceived of as liability-expenses. Asset expenses, as we use the term, mean the salaries of bookkeepers and of the clerks who cut coupons and attend to the details of purchase and sale of securities. Liability-expenses mean the salaries of the same bookkeepers and of the clerks who attend to the creation and discharge of liabilities, including taxes, and the sums ordinarily and necessarily paid to lenders by way of interest or other compensation. In point of fact, the deductibility of all these asset-and-liability-expenses is conceded by the Government, *except* that which is the most ordinary and most necessary of all of them, i. e., the exaction by the creditor of the price of the loan. The business man might, conceivably, himself handle his assets without expense, but he cannot do this with his liabilities. He cannot get his creditors to forbear the enforcement of their claims unless

he pays them their stipulated compensation. It is a short-sighted and unreasonable governmental policy which recognizes the business of producing wealth and taxes the wealth when produced, and yet refuses to concede the deduction of the ordinary and necessary expense of preserving the assets from erosion by liabilities. As to the point under consideration (i. e., what are lawfully deductible expenses) the authorities relied upon by the petitioner are analyzed and discussed in Appendices I and II. Four cases in particular appear to be relied upon as the basis of petitioner's argument. All four of these seem to us to deal with questions entirely distinct from the issue in the instant case.

Two of these cases are *Dalton v. Bowers,* 287 U. S. 404 (1932), and *Burnet v. Clark,* 287 U. S. 410 (1932). In the former, the taxable made contributions to the capital of a corporation which he had formed and also voluntarily paid some of its obligations. When the corporation failed, he attempted to deduct the aggregate of these contributions and payments as *losses* incurred in *his* business. There was no suggestion that he was engaged in the business of conserving and enhancing his estate. Mr. Justice McReynolds, speaking for the Court, said (see page 409 at bottom):

> "Dalton (the taxable) was not regularly engaged in the business of buying and selling corporate stocks . . . Ownership of all the stock is not enough to show that creation and management of the corporation was part of his ordinary business."

The decision was that the business was not *his,* but the corporation's, that the only business losses were its losses and that his losses were not business losses at all.

In *Burnet v. Clark,* the taxable was merely a stockholder in a corporation and was specifically found *not* to

be in the business of endorsing notes or buying and selling securities. He did, however, endorse the notes of the corporation and sustained losses as the result of selling its stock. He claimed that he was entitled to deduct *as losses* the amounts which he spent to pay the corporate obligations and to meet the liability on account of the stock. Held, that *he* was not in business at all and, therefore, could not claim deductions for business losses.

In the third case, *Burnet v. Commonwealth Improvement Company,* 287 U. S. 415 (1932), securities had been exchanged between testamentary trustees and a corporation which was, in effect, the incorporated estate of the decedent. On the exchange, the corporation made a gain which was held to be taxable, notwithstanding the substantial identity of the parties to the exchange.

We respectfully submit that we are justified in saying that the foregoing three decisions have nothing to do with the instant case. The facts are different. The deduction, where it was claimed, was claimed on a different ground; and in none of them was the taxable engaged in the business of conserving and enhancing his estate, nor was it shown that he was engaged in any other business.

The fourth case, likewise distinguishable, is *Welch v. Helvering,* 290 U. S. 111 (1933). Here the taxable stood in such a business relation to a corporation that its bankruptcy and consequent failure to satisfy creditors constituted a menace to his personal credit and standing. He, accordingly, paid some of the corporate debts, although he was not liable for them. He attempted to deduct the sums so paid as ordinary and necessary expenses of *his own* business. The deduction was refused on the ground that what he had paid was really a capital outlay, i. e., a sum

paid to purchase goodwill. However "necessary" in a business sense, such a payment was not "ordinary" and, therefore, could not be allowed. To mark the distinction between the *Welch* case and the instant case, it is only necessary to observe that in the former, the taxable was paying debts he did *not owe*, in order to purchase a capital asset, goodwill; whereas here, appellant, by paying carrying charges on an obligation which he *did* owe, paid a current expense of the business in which he was engaged.

We submit not only that the cases relied upon by the petitioner are clearly distinguishable from the instant case but that the nature of the contrast in each instance supplies collateral support to the contention that the origin of the liability upon which respondent paid carrying charges is wholly irrelevant to the deductibility of the expense of carrying the loan which discharged it.

3. The expenditure necessary to carry the new loan was the price of the lender's forbearance; and the payment of this price was in its nature "interest on indebtedness" notwithstanding that the subject-matter of the indebtedness was stock and not money.

"It may well be" said Judge Maris "that the expenditure which the plaintiff (respondent) made in this case was a payment of interest in the broadest sense. It is certain, however, that it was compensation for the loan of stock which he had made and as such it was an ordinary and usual expense of a transaction of that character. Dart *v.* Commissioner of Internal Revenue, 74 F. 2d 845."

The opinion of the Circuit Court of Appeals thus indicated was that the sums claimed as deductions were certainly expense payments and might well be regarded as

interest payments. We submit that whether or not these payments would have been deductible had the statute permitted the deduction of expenses only, they are clearly deductible under the provision of the statute applicable to interest.

It will be remembered that in computing his taxable income for the year 1931, the respondent deducted from gross income, two items of expenditure admittedly made by him in that year.

One was an item of $567,648. The other was an item of $80,083. Both these sums were paid by him to a corporation styled the Delaware Realty and Investment Company. Both were included by that corporation in its income tax return, and the appropriate tax thereon was paid to the Federal Government. In other words, the story begins with the collection by the Federal Government of at least one tax on the transaction.

On the theory that the money so received by the corporate taxable was taxed as *interest received by it*, respondent figured that it must also have been *interest paid by him*. He, accordingly, deducted it under that provision of the Revenue Act, which allows a taxable to deduct:

> "All interest paid or accrued within the taxable year on indebtedness,"

with an exception not at the moment important. The Bureau of Internal Revenue allowed this deduction for the first eleven taxable years in which it was claimed.

It is, of course, not legally relevant that, unless the deduction thus claimed is allowed, the Federal Government will have received two income taxes on the same income within the same year. Even if this be double or multiple taxation it is not per se illegal. The petitioner's brief mis-

conceives the contention of the respondent on this point. We are mentioning it not as an argument against the legality of the tax in question but merely to overcome the unfavorable presumption which arises if it appears that the transaction in issue would escape taxation altogether if the Government's contention were not sustained. The payments have, in fact, been made and received, and the sum of them has been reflected in the amount of tax paid by the receiver. The only question is whether the payor is likewise to be made taxable with respect to them by a denial to him of the right to deduct them from his gross income.

If a wealthy taxpayer is trying to give to the exempting language of a statute a meaning so broad as to defeat its reasonable operation, a court may properly insist on strict construction and so effectuate the legislative purpose. In the instant case, however, it is not reasonable to suppose that the Congress, for any substantial reason, intended to refuse deduction of interest on a loan of stock while permitting its deduction in the case of a loan of money.

Our first proposition, on this branch of the case, is that the obligation of a borrower to the lender in the case of a loan of stock is an *indebtedness* within the meaning of the Revenue Act.

It is sometimes considered an affectation of learning to refer to the Roman law. But, after all, it, rather than the common law, is the source of our commercial conceptions; and "indebtedness" is, itself a Latin word. It is, therefore, worth noting that according to the general commercial law, the significant distinction is not between loans of money and loans of other things, but between loans which, on the one hand, impose an obligation to return the very thing that is lent, and on the other, those in which

the obligation of the borrower is satisfied by returning an equivalent for the thing lent—whether it be money, or corn, or wine, or oil, or (as in this case) stock. This latter form of loan was the Roman *mutuum*, and such was the precise transaction between the respondent and the Delaware Realty and Investment Company.

The following illuminating quotation from a work of high authority will make this clear:

> "Things which are estimated by weight, number or measure, and cannot be used without being consumed, become the property of the borrower, subject to the obligation of returning a like amount identical in kind though not in substance. For as the loan must under these circumstances remain idle, or be employed in a way that precludes the possibility of its being returned in specie, the parties may fairly be presumed to have contemplated the latter alternative. It needs no argument to prove that if I lend my neighbor a hundred dollars, they are as much his as if they were given absolutely; and the resulting duty is not to return the very coins or bank-notes, but as many dollars as will make up the sum.
>
> "It is, therefore, essential to the validity of a *mutuum* that the things lent should be of such a nature that the return of a like quantity will presumably be an equivalent; because the contract would otherwise be an exchange instead of a loan. Money is obviously within this category; and it also includes corn, wine, oil and other articles which are ordinarily sold by count, weight, or measure. But the criterion is not conclusive; and the loan of a book will not be regarded as a *mutuum*, in the absence of an agreement to that effect, although one copy of the edition may be as valuable as any other, because it may be read and returned in the same condition." (The Law of Contracts by J. I. Clark Hare, p. 73.)

That the obligation of the borrower in such a transaction as above described is strictly an indebtedness is beyond reasonable doubt. Indebtedness is coextensive with obligation; and an obligation covers all cases in which B. is personally bound to A. to render him some thing or service. (Hare, p. 64.)

In the case of a *mutuum* (i. e., a loan to be repaid in kind), the borrower is strictly a debtor and his obligation to repay in kind is uniformly styled a debt in all standard works on Roman law. See, for example, Ledlie's Sohm's Institutes of Roman Law (2d Ed.), p. 395.

The scope of the term "indebtedness" has never been narrowed in popular usage. "I am deeply indebted to you," is a familiar form of expression to indicate a sense of obligation to make some suitable return for a kindness shown, a favor done or a service rendered.

It is in the broad sense of obligations unperformed that in the Lord's Prayer, we ask to be forgiven our "debts"; and in the original meaning of "debt" are included obligations *ex delicto* as well as those otherwise arising. (Hare, p. 65.) The Court is also referred to the following definitions taken from Webster's New International Dictionary:

> "Debt. 1. That which is due from one person to another, whether money, goods or services; that which one person is bound to pay to another or to perform for his benefit; the thing owed; obligation; liability."
>
> "Indebtedness. 1. State of being indebted. 2. The sum owed; debts, collectively."

These definitions of "indebtedness" as applicable to a "short-sale" of stock are in accord with a recent decision of the Circuit Court of Appeals for the Third Circuit

in *Henry B. du Pont v. Commissioner*, 98 F. (2d) 459 (1938). In that case Judge Biggs adopted the theory advanced by us in the instant case and quoted one of the authorities as follows:

> "James Edward Meeker, Economist to the New York Stock Exchange, states in his book 'Short Selling,' 'A short sale may be briefly but comprehensively defined as a sale which creates a debt in terms of goods.' The sales made by the petitioner from April 15, 1930 to November 19, 1932, inclusive, are precisely within the definition given by Meeker."

Assuming, as established by reason and authority, the proposition that the obligation of the respondent to the Delaware Realty and Investment Company is an indebtedness, our second proposition is that the compensation for the loan which the borrower bound himself to pay during its life is "interest" within the meaning of the Revenue Act.

Here, again, it is helpful to return to first principles. Authorities are unanimous to the effect that the obligation of the borrower to restore the equivalent of what he has received may include an obligation to pay compensation for the loan and that this compensation so stipulated for is styled "interest", whether it be compensation for the use of money or for the use of other fungibles. It is of special significance that, according to the Roman law, a separate enforceable contract was necessary to bind the borrower to pay interest on a loan of *money*, but that in the case of a loan of any other fungibles, the later Roman law treated an informal agreement for the payment of interest, although a mere *nudum pactum*, as sufficient to create a legal duty to pay such interest. (See Sohm, p. 395.) In other words, according to the Roman system, the payment of in-

terest on a debt other than a debt for money was an obligation which might be entered into more lightly and more informally than an obligation to pay interest on a money debt. Irrespective of the subject-matter of the loan, therefore, it is clear beyond reasonable doubt that the classical meaning of "interest" has always included compensation for the use of the thing borrowed.

It is true that the District Court justified its decision to the contrary, by referring to the popular tendency to restrict the classical conception of interest to compensation for the use of money. In so doing, however, we suggest that the learned Court really begged the question at issue. If we are right in insisting that the obligation of the borrower of the stock is properly classified as an indebtedness and that "interest" in its classical sense means the lender's return on every form of indebtedness including this one, then the real question is whether we should impute to the Congress the intention to substitute the narrower popular meaning for the broader classical usage when inherent reasonableness requires the use of the latter.

Strangely enough, the District Court in seeking judicial justification for narrowing the term "interest" as applied to a *mutuum*, cited *Old Colony R. R. v. Commissioner*, 284 U. S. 552 (1932), where, in fact, no such question was in issue. That case was one in which the borrower of (say) $1,100. had issued an obligation which he could discharge at maturity by paying $1,000. The obligation specified that the holder was entitled to 5 per cent. interest, or some other named rate; the report does not seem to show exactly what it was. The question in substance was whether the borrower might properly deduct the entire 5 per cent. as interest on indebtedness, or only that fraction of 5 per cent.

(10/11ths) applicable mathematically to the face value of the bond. The obviously sound decision was that in such a case, the Congress doubtless intended to allow the deduction of anything in fact paid as interest on the indebtedness and did not intend to distinguish between par and premium. It is therefore evident that the decision dealt with the scope of "indebtedness" rather than with "interest"—holding that the contract rate should be applied. It is noteworthy, however, that the Supreme Court in that case applied to the interpretation of a deduction the same canon of liberal construction in favor of the taxable which is the general rule in the interpretation of taxing statutes. The Court said: "If there were doubt as to the connotation of the term and another meaning might be adopted, the fact of its use in a tax statute should incline the scale to the construction most favorable to the taxpayer," citing five United States Supreme Court decisions. In that case, as in the case at bar, the taxpayer, in order to arrive at his net taxable income, was attempting to deduct from his gross income an item of interest paid by him.

In addition to the foregoing considerations, it may be questioned whether there *is* any such uniform popular conception of "interest" as was assumed by the trial court. It is quite common to hear dividends referred to as interest, especially dividends on preferred stock. It is common in New England to speak of "hiring" money, which indicates how close is the popular conception of compensation for the loan of money and compensation for the loan of things which must be specifically returned.

However, we do not need to go so far as to urge that rent paid by a bailee for the use of a tangible chattel would be deductible as interest under the statutory provision. In the case of a bailment, e. g., of an automobile, the bailee is

expected to return to the bailor the identical chattel borrowed and the consideration he gives for the use of the chattel is ordinarily designated as rent. In such a case, the title to the chattel lent remains in the bailor. In the case of a loan of money the situation is quite different. Title to the particular currency lent passes from the lender to the borrower for the very purpose of permitting the borrower to transfer title thereto to others. The very purpose in borrowing money is that the borrower may spend it. The lender knows this in transferring title to the borrower and expects to be repaid with other money of similar value. The loan of stock in the case at bar is exactly similar to the loan of money. The lender of the stock transferred complete title to respondent with full knowledge that it was his purpose forthwith to retransfer that title to others and eventually to repay his debt, not with the same certificates, but with other certificates representing an equivalent number of shares in the same company.

Should respondent default in his obligation to return to the Delaware Realty & Investment Company, 142,212 shares of du Pont common stock at the expiration of the ten-year period, the remedy of the Delaware Company would not be by replevin or bill for the specific performance of the contract, requiring him to procure such shares and deliver them, but by an action for money damages. The lender could either purchase the stock in the open market and hold respondent for the purchase price, or sue him for the market value of the shares. The judgment in either event would be for a sum of money.

Thus, both our present law and the Roman law place the loan of fungible goods, where the specific goods are not to be returned, in a class separate and apart from those

loans where the specific property is to be returned. Historically, the compensation of the lender for all the loans of the first type has been called interest, and there is no basis for now claiming that the word "interest" applies only to loans of money.

All that has been said about compensation for a loan of something other than money is peculiarly applicable to a loan of stock, where the measure of the compensation is the sum of the dividends declared on it and the tax that becomes payable with respect to it. Note the following quotation from Van Leeuwen's Roman Dutch Law, 2d ed., Vol. II p. 55:

> "That which is stipulated for the benefit of property or money lent is commonly called *interest* or money-profit (because it generally consists of money); for here, besides the return of the same thing of the like kind and quality, we also stipulate for what we lose through being deprived of the thing or money."

This court has approved a definition of interest equally broad. In *United States v. North Carolina*, 136 U. S. 211, 216 (1890), in an opinion by Mr. Justice Gray appears the following:

> "Interest, when not stipulated for by contract, or authorized by statute, is allowed by the courts as damages for the detention of money or of property, or of compensation to which the plaintiff is entitled."

In the light of these authorities it is interesting and important to compare the language of the Revenue Act of 1928 with other legislation of Congress dealing with the subject of interest. In Appendix III, B, we have cited the Code of the District of Columbia, Title 17, Chap. 1, Section 1, dealing with the rate of interest in the District of Columbia and have added references to many earlier statutes, both

in the United States and in England, each dealing with the same subject. A study of them seems to us to make it clear that historically the term "interest" is applicable to the price of forbearance on loans of property other than money, and to suggest that as a matter of inherent reasonableness no narrower definition should be given to the term as used in the Revenue Act of 1928. Among other points covered in Appendix III is the distinction between the scope of the terms "interest" and "usury". To the extent that the exaction of usury is either a crime or a ground of forfeiture there are reasons for confining the conception to loans of money which are entirely absent when nothing but the simple conception of interest is under consideration.

The Government makes much of the decision in *Terbell v. Commissioner*, 29 B. T. A. 44. This case was decided by the Board of Tax Appeals before its decision in *Dart v. Commissioner*, 29 B. T. A. 125. It held that the carrying charges on a short sale were not business expenses because it did not appear that the taxpayer was in business. The Board did not seriously consider the interest question, giving on this subject merely the *ipse dixit* "It is clear that the sum of $22,500. paid to the lender of the stock was not interest *per se*, and the petitioners did not seriously contend that it is." A decision rendered in the absence of serious contention is not ordinarily regarded as authority. A month later the Board decided the *Dart* case (29 B. T. A. 125) without distinguishing the *Terbell* case but relying upon it as authority.

The *Terbell* case went to the Circuit Court of Appeals for the 2d Circuit, which affirmed the Board (71 F. 2d, 1017) in a per curiam opinion, citing only three cases, which are related to the question of distinction between capital ex-

penditures and expense items, none of which involved carrying charges.

When the *Dart* case reached the Circuit Court of Appeals the Government relied on the same authorities as in the *Terbell* case. The Court nevertheless reversed the *Dart* case. Now the Government insists that the *Dart* case and the *Terbell* are distinguishable and that the instant case should be assimilated to the *Terbell* case and distinguished from the *Dart* case.

In view of the foregoing considerations, this Court is earnestly urged to treat as unjustifiably narrow any interpretation of "interest" as used in the Revenue Act which limits it to money loans. We submit that the money paid by the respondent to the lender of the stock was, both on principle and authority, money paid as interest and, as such, deductible under the terms of the Act of Congress.

We are not overlooking the fact that the amount of compensation to be paid was not, in this case, predetermined by reference to a specified rate. The importance of a specified rate is merely to supply a definite measure of the lender's claim and the borrower's liability. This clearly appears in cases where one lends money to partners and stipulates for a share of profits as interest on the loan. Nobody will dispute the proposition that if the transaction is clearly one of lending, the receipt of a share of profits is regarded as a receipt of interest; and such participation in profit does not constitute the lender a partner. Both on principle and authority, therefore, that which is in its nature interest will none the less be regarded as interest merely because it is measured by some other standard than a predetermined rate.*

* In *Cammack v. United States*, D. C. Minn., 3d Div. May 22, 1939, P-H ¶ 5.453, C. C. H. ¶ 9534, Kreuger & Toll

4. Since the claimed deductions are only carrying charges and not the principal of the loan, it should seem that the nature of the original debt which was discharged by the loan is really unimportant; but if and when it is scrutinized, it will be found to have been in fact a debt incurred to conserve and enhance the respondent's estate.

The facts, in brief, were these:

In the year 1919, respondent being the beneficial owner of 95,139 shares, approximately one-sixth, of the total outstanding common stock of the du Pont Company, had a correspondingly direct interest in conserving and enhancing the value of his holdings. At this time the company's officers decided to establish a more permanent community of interest between the company's shareholders and nine important executives by making it possible for the latter to acquire 1000 shares apiece of the company's stock. The

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"American Certificates" carried interest at 5 per cent. plus 1 per cent. for every 1 per cent. paid on ordinary shares in excess of 5 per cent. The Commissioner and the Court treated these certificates as evidences of indebtedness. Could it be doubted that the extra percentage is interest, as much as the fixed 5 per cent.? If so, would the situation be any different if there were no fixed 5 per cent.? Cf. United States savings certificates, sold at a discount from face with the condition that they may be surrendered before maturity with specified increases over sale price, but, if held to maturity, will be paid off with a substantially larger increase over sale price.

Specified times for payment of interest are not necessary. Judgments bear interest until discharged. Debenture bonds accrue interest according to time, but it is only payable when earnings are available. (*H. R. de Milt Co.*, 7 B. T. A. 7.)

A definite time for maturity of principal debt is not necessary—e. g. British "Consols."

company found, however, that there were no shares available for the purpose. It was then that the respondent, perceiving that the proposed step would obviously conserve and enhance the value of his du Pont stock and would put him in possession of a large amount of cash, offered to sell the necessary 9000 shares to the nine executives at their then fair value, which by appraisement was determined to be $320. per share. This offer was accepted. In order to make delivery under his contract respondent borrowed the shares from the Christiana Company, which company was itself a large holder of shares in the du Pont Company.

At this point we wish to emphasize a distinction (overlooked we think by the petitioner) between the transaction of sale to the executives and the transaction of borrowing stock to cover that sale. The respondent contends that in the former transaction one of his primary motives was to conserve and enhance the value of his heavy holdings of shares in the du Pont Company. As a legal proposition he insists that the presence of this motive gives character to the transaction of sale as a step taken in the course of his personal business. Quite apart from this contention, although wholly consistent with it, is the contention which we earnestly press upon the consideration of the Court that the respondent's ONLY motive in borrowing stock to cover his short sale was a business motive, i. e., his wish to use the entire purchase money in the profit-making ventures in which he forthwith proceeded to embark.

Let us first give our reasons for thinking that the sale to the executives was a step taken by respondent in enhancing and conserving his estate.

The fallacy in the argument to the contrary consists in assuming that because the transaction with the nine

executives was of advantage to the Company, it could not have been a transaction made in the course of the respondent's business. This is a palpable non sequitur.[1] If it was good business for the respondent to incur expense in order to create a community of stock interest between himself and others, it does not cease to be good business for him merely because the du Pont Company was correspondingly benefited. If a taxable engaged in the business of conserving and enhancing his estate were to make a handsome contribution to the Red Cross, he certainly would be permitted to treat it as a charitable gift, although the favorable publicity incident to it might greatly improve his standing and credit. In other words, the immediate and necessary character of a disbursement is not changed (so far as the payor is concerned) merely because by making it he succeeds in killing two birds with one stone.

If respondent *not* being in the business of conserving and enhancing his estate, had been a stockholder in a corporation which got into difficulties and he had made fruitless payments to help it out; and if, on such a state of facts, he had attempted to deduct the amount of these payments as losses, the decision would have been against him because the losses were not incurred in his business but in the business of the corporation. Such would be the effect of the above-cited decisions in the *Dalton* case and the *Burnet* case. Or, if the respondent, being in the business of conserving and enhancing his estate, had voluntarily paid the debts of a corporation bearing his name and had attempted to treat such payments as expenses currently incurred in the course of his own business, he would have been met with the decision in the Welch case, to the effect that money

[1] Cf. Bonwit v. Commissioner, Appendix II, p. 8a.

thus spent to purchase goodwill is not an ordinary expense and is, in any event, a capital outlay.

Or let it be supposed that the respondent had had no interest whatever in the du Pont Company, but had a very real and friendly interest in each of the nine young men in the employ of that corporation. Suppose, further, that to promote their welfare, he had generously made an expenditure in order that they might make advantageous purchases of the Company's stock. These payments certainly would not have tended to conserve or enhance his estate. They would have tended to conserve and enhance the business of the Company, but this circumstance would have given him no right to deduct them. We respectfully submit that the same conclusion as would be reached in this supposititious case cannot possibly be justified upon the facts of the actual case, unless a definition of conservation and enhancement is to be adopted so narrow and unreasonable as to be purely arbitrary.

Nor is the Government helped by the circumstance that when the fall in value of du Pont stock threatened to discourage the nine executives instead of to stimulate their interest, respondent voluntarily indemnified them against resulting loss while making it possible for them also to secure an enhanced profit. The business significance of this transaction is obvious. It was the act of a large-minded and far-seeing business man, who was willing to make a very heavy payment to prevent the failure of a plan in which he had already invested a large sum of money. He is not contending that the value of the shares of Christiana stock given by him to the nine executives to protect them against loss incident to the shrinkage of du Pont stock was deductible as an ordinary expense of his business, although it was in fact an expenditure made to retain the

interest and goodwill of the nine employees for his own pecuniary benefit rather than have it turn into ill-will, as might have been the case if their great expectations had been turned into disappointment.

In contrast to these supposititious cases we submit that what the respondent in the instant case actually did was to make a sale of some of his shares of du Pont stock for the sake of conserving and enhancing the value of the many thousand shares of the same stock of which he continued to be the beneficial owner. We urge that the presence of this motive is an irresistible inference from the facts and is quite sufficient to mark the transaction as an excellent piece of business.

If, however, it be assumed (but only for the sake of the argument) that the transaction of sale was not a transaction in the course of respondent's business, we press upon the consideration of the Court the second of the two contentions above referred to, namely, that the decision to borrow stock to cover the sale instead of using other available shares for that purpose was a decision that could have been dictated by no other motive than a desire to make a business profit out of another use of the entire purchase money yielded by the sale.

At that time the respondent was the beneficial owner of 24,000 shares of du Pont stock which had been placed temporarily in two trusts in order to provide funds for building schools and a hospital (Exs. N, O, P;—R. pp. 75-90). Ten thousand of these shares were available to the respondent at any time upon payment of not to exceed $600,000. (Exs. N, O;—R. pp. 75-84) cash to the trustee for their release. These shares and 14,000 other like shares were also available to the respondent by substitution of other securi-

ties for the purposes of the trust. It was asserted below, and no doubt will be argued by the petitioner here, that this transaction with the nine executives was not entered into for the purposes of profit. There is a finding of fact to this effect (No. 17). But this merely means that the respondent contemplated no profit at the expense of the executives. The fact just stated that for an expenditure of $600,000. (less than one-fourth of the purchase money received from the executives) he could have redeemed his own shares and delivered them under his contract is sufficient evidence that there was in fact a profit-motive in borrowing the stock from Christiana instead of acquiring it with the money he received. That this is not mere matter of inference appears from a reference to a case several times cited in the petitioner's brief, namely, *du Pont v. Commissioner*, 37 B. T. A. 1198.

On page 30 of petitioner's brief will be found the following quotation from the opinion in the case so cited:

> "We therefore cannot disregard the setting, the reasons for entering into the transaction for borrowing stock; to do so would leave before us a mere borrowing, isolated from the business which we have assumed petitioner to be carrying on. . . ."

It appears from du Pont's income tax return for 1929 (Ex. R-139 in the cited case—Vol. 4 p. 274 of the record in No. 7044, C. C. A. 3; Oct. term 1939) that he was a heavy buyer of General Motors stock during the year 1921; and it further appears that in the year 1929 the taxable sales of that stock produced to the respondent a profit of $36,807,161.73, a transaction which resulted in a tax, duly paid, of approximately $4,500,000. In the light of these

inescapable facts it requires something like temerity to argue that the decision to borrow du Pont stock and then to sell it for its fair value in cash was merely a philanthropic transaction wholly devoid of the profit motive.

The contract of borrowing, which was to run for ten years, called for the periodic payment by respondent to the lender of amounts equal to the dividends declared on the borrowed shares. These sums he regularly paid. As and when received by Christiana, they were taxable as part of that company's income and, year after year, he deducted them from his gross income in making his personal Income Tax returns. The deduction by the respondent of these annual payments equal to the dividends declared on the borrowed shares was allowed by the Government for eleven taxable years, until the Board of Tax Appeals, in 1933, decided *Dart v. Commissioner*, 29 B. T. A. 125. The Board held that a person engaged in a business of buying and selling securities, who sold certain stock "short" through brokers, might not deduct as ordinary and necessary expenses, charges in his account made by the brokers for dividends paid by them on certificates which they had borrowed for delivery to the purchaser. The Board of Tax Appeals treated the amount of these dividends as a capital expenditure which entered into the cost of the stock and should be included in the cost to determine the profit or loss on the short sale. If the *Dart* case and the present case were analogous, and if the decision in the *Dart* case had been correct, the conclusion of the Government, with respect to the respondent's 1931 tax return, would also have been correct. The Government, specifically in reliance upon that decision (R., p. 165) announced a change in its policy and declined to permit the respondent to make, in his 1931 tax return, deductions similar to those

allowed in earlier years. In point of fact, however, *Dart* appealed, and in *Dart v. Commissioner*, 74 Fed. (2d) 845 (1935), the Circuit Court of Appeals for the Fourth Circuit reversed the Board of Tax Appeals and held that such dividends constituted ordinary and necessary expenses. The Government did not appeal from this decision. It, accordingly, appears to be clear that if the Circuit Court of Appeals for the Fourth Circuit had been called upon to decide the instant case, the deductions now claimed by the respondent would unquestionably have been approved, unless that Court were to give less favorable treatment to one diligently engaged, as is the respondent, in enhancing his estate by sound business methods, than was given in the *Dart* case to one who was engaged in speculation, as a side issue to his tobacco business.

In the foregoing discussion we have assumed that this Court will regard the decision of the Circuit Court of Appeals for the Fourth Circuit in the *Dart* case as sound. If, however, the Court regards that decision as for any reason questionable, we respectfully refer to Appendix II to this brief. We have there discussed with care the principles which seem to us to distinguish expense items from capital outlay and to vindicate the soundness of the decision in question. In spite of the petitioner's attempt to distinguish the *Dart* case, we submit that it is a clear authority for the proposition that the carrying charges sought to be deducted in the instant case are items of expense and as such are deductible under the statute.

Conclusion.

There is such a "trade" or "business" as the conservation and enhancement of a taxpayer's estate; and, as the trial court expressly found, the respondent was primarily

engaged in it. No serious contention to the contrary can be made. The deductions claimed by the respondent were properly allowed by the Circuit Court of Appeals upon the ground that they were items of current business expense. They might equally well be allowed upon the additional and consistent ground that they were payments by way of interest on indebtedness paid and accrued within the taxable year. It follows that the judgment of the Circuit Court of Appeals should be affirmed.

Respectfully submitted,

JAMES S. Y. IVINS,
GEORGE WHARTON PEPPER.

APPENDIX I

APPENDIX I.

APPENDIX I.

AUTHORITIES ON QUESTION WHETHER MANAGING INVESTMENTS CONSTITUTES A BUSINESS.

In *Flint v. Stone Tracy Co.*, 220 U. S. 106, 171, the Supreme Court adopted the definition from Black's Law Dictionary, "'Business' is a very comprehensive term and embraces everything about which a person can be employed", and also the definition from Bouvier's Law Dictionary, "'That which occupies the time, attention, and labor of men for the purpose of a livelihood or profit' ".

In *Von Baumbach v. Sargent Land Co.*, 242 U. S. 503, 515, the Court referred back to *Flint v. Stone Tracy Co.*, and said:

> it became necessary to inquire what it was to do business, and this court adopted with approval the definition judicially approved in other cases, which included within the comprehensive term "business" "that which occupies the time, attention, and labor of men for the purpose of a livelihood or profit."

In *Karnuth v. United States*, 279 U. S. 231, 243, the Court said:

> The word is one of flexibility; and, when used in a statute, its meaning depends upon the context or upon the purposes of the legislation.

The provision for deduction of ordinary and necessary business expenses contained in section 23 (a) of the Revenue Act of 1928 and subsequent Revenue Acts, was the same as the provision in prior Revenue Acts back to that of 1918.

The Treasury Department has been consistent in its rulings that the management of investments, if occupying a substantial amount of the taxpayer's time, constitutes a business, and that the expenses of such management are deductible from gross income. In 1921 the Treasury Department published Office Decision 877, 4 C. B. 123, which reads as follows:

> A taxpayer whose income is derived principally from investments in stocks and bonds may deduct as a business expense the rent of an office and the cost of clerical help if he can show in his return that such expense is ordinary and necessary within the meaning of section 214 (a) 1 of the Revenue Act of 1918.

There was no departure from this ruling between 1921 and 1934, when I. T. 2751, XIII-1 C. B. 43, was published, which reads as follows:

> Revenue Acts of 1918, 1921, 1924, 1926, 1928, and 1932.
>
> The ordinary and necessary expenses paid or incurred during the taxable year with respect to the management, protection, and conservation of properties producing taxable income are deductible from gross income.
>
> The question has been presented as to the deductibility of fees and expenses paid in connection with the management, protection, and conservation of various income-producing properties.
>
> The Revenue Acts have consistently provided for the deduction of "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." (Section 23 (a), Revenue Acts of 1932 and 1928, and section 214 (a) 1, Revenue Acts of 1926, 1924, 1921, and 1918.) This provision of law has been liberally construed as disclosed by the following decisions:

In Office Decision 877 (C. B. 4, 123) it was held that a taxpayer whose income is derived principally from investments in stocks and bonds may deduct as business expenses the rent of an office and the cost of clerical help if he can show that such expenses are ordinary and necessary.

Fees, commissions, and other compensation of committees for incompetent persons, as well as expenses properly incurred by such committees, have been held to be allowable deductions for income tax purposes if paid or incurred with respect to the management or conservation of income-producing property or funds belonging to the incompetent or with respect to the collection or securing of any income inuring to such incompetent. (I. T. 2238, C. B. IV-2, 49.) It has also been held that if a safety deposit box is used primarily in connection with the safeguarding of income-producing securities, the rent paid therefor constitutes a deductible business expense. (I. T. 2579, C. B. X-2, 129.)

The Board of Tax Appeals has consistently held that expenses paid or incurred in preserving an estate, making sales and collections, and doing other things necessary for the maintenance of the estate and the production of income, are ordinary and necessary expenses, and therefore proper deductions in computing net income. (*Appeal of Grace M. Knox et al.*, 3 B. T. A. 143, C. B. X-2, 39; *Appeal of William W. Mead et al., Exs.*, 6 B. T. A., 752, C. B. X-2, 47; *Appeal of H. Alfred Hansen, Ex.*, 6 B. T. A., 860, C. B. X-2, 29; *Henrietta Bendheim v. Commissioner*, 8 B. T. A., 158, C. B. X-2, 6; *George W. Seligman, Ex., v. Commissioner*, 10 B. T. A., 840, C. B. X-2, 64.)

In the case of *Kenan et al. v. Bowers* (48 Fed. (2d), 263), the court held that compensation for clerk hire and rent of a safe in connection with the taxpayer's income-producing property were deductible.

The foregoing decisions indicate an obvious intent to allow as deductions all the ordinary and necessary expenses paid or incurred in the production of taxable income. This principle rests upon the sound basis that business expenses represent the cost of producing income.

In view of the foregoing, it is held that all the ordinary and necessary expenses paid or incurred during the taxable year with respect to the management, protection, and conservation of properties producing taxable income should be allowed as deductions in computing net income. In this connection care should be taken to distinguish expenditures of a capital or personal nature. This conclusion should not be extended to net loss cases, which are governed by different sections of the Acts and apply only to losses incurred in a trade or business regularly carried on by the taxpayer.

The Commissioner of Internal Revenue published acquiescences not only in the Board decisions enumerated in I. T. 2751, above, but in subsequent decisions of the Board of Tax Appeals similarly holding that expenses incurred in preserving an estate are deductible. For example, in 1939 (I. R. B. 1939-1-9655), the Commissioner acquiesced in the Board's decision in *Austin D. Barney, et al.*, 36 B. T. A. 446, and later in 1939 (I. R. B. 1939-4-9683) the Commissioner acquiesced in the Board's decision in *George S. Groves v. Commissioner*, 38 B. T. A. 727.

The long continued departmental construction would of itself justify the courts in following the rulings of the Treasury Department. *United States v. Johnston*, 124 U. S. 236.

When coupled with re-enactment of the statute in similar terms, the departmental construction is regarded as adopted by Congress. *National Lead Co. v. United States*, 252 U. S. 140, 145; *Helvering v. Winmill*, 305 U. S.

79. A recent case involving this very construction of this same section of the statute is *Kales v. Commissioner* (C. C. A. 6, January 12, 1939), 101 F. (2d) 35, 38, where the court said:

> It has long been a recognized rule of statutory construction that the re-enactment of a statute by Congress in identical terms and failures to amend it in the face of consistent judicial and administrative construction is persuasive of a legislative recognition and approval of the statute as thus construed. Brewster v. Gage, 280 U. S. 327, 50 S. Ct. 115, 74 L. Ed. 457; Helvering v. Bliss, 293 U. S. 144, 151, 55 S. Ct. 17, 79 L. Ed. 246, 97 A. L. R. 207. A long series of Treasury decisions were promulgated before the passage of the 1928 Act defining "business" with substantially the breadth given to it in Flint v. Tracy Stone Co., supra, yet § 23 of that Act re-enacted similar provisions of § 214 of the Acts of 1918, 1921, 1924 and 1926, 40 Stat. 1066, 42 Stat. 239, 43 Stat. 269, 44 Stat. 26. More important still is the fact that while the Kissel Case was decided by the Board of Tax Appeals in 1929, and the von Echt Case upon rehearing in 1932, § 23 (a) was retained without change in the 1932, 1934 and 1936 Acts, 26 U. S. C. A. § 23. We are asked by respondent's counsel to view the conflict between the Board's decision in the instant case and those in the Kissel, von Echt and other cases as merely indicating "some inconsistency and vacillation" rather than as departure from a hitherto consistently maintained construction. But that the respondent finally acquiesced in the rule of the von Echt and Kissel Cases is indicated by the lack of any citation on appeal, and in the formal response of the Bureau to the inquiry of the Committee of Banking Institutions on Taxation (reported in Standard Federal Tax Service 1934, Vol. 3, § 6035) in which it was said: "You direct attention to the reconsideration by the United States Board of Tax Appeals of the case of Alice P. Bachofen von Echt v. Commis-

sioner, 21 B. T. A. 702, reference to which is made in the letter addressed to you on August 19th, 1933. You are advised that the Bureau has recently adopted the policy of allowing as a deduction all the ordinary and necessary expenses paid or incurred during the taxable year with respect to the management, protection and handling of properties producing taxable income." The situation here outlined calls for the application of the rule of Brewster v. Gage, supra.

Although the last published Treasury ruling—I. T. 2751, set forth above, p. 2a, stands unrevoked and is broad enough to cover all cases where expenses are incurred in the management, protection and conservation of properties producing taxable income, the Bureau of Internal Revenue has nevertheless contested deductions in a number of cases where the taxpayer was said to be a "mere passive investor" not being sufficiently active in his affairs to justify calling his managerial efforts a business. In a number of these cases, the courts and the Board of Tax Appeals have held that, on the particular facts, they did not regard the taxpayer as carrying on a business and have denied the deductions on that ground. The cases cited by the Government in support of its proposition that (contrary to the finding of fact of the District Court) Mr. du Pont's efforts, occupying 50 per cent of his time, in the management and conservation of his investments did not constitute a business, are cases of this type.[1] In the opinions in most of them the courts recognized that the conservation and management of investments *may* constitute a business but dis-

[1] *Van Wart v. Commissioner*, 295 U. S. 112; *Monell v. Helvering*, 70 F. (2d) 631; *Kane v. Commissioner*, 100 F. (2d) 382; *Kenan v. Bowers*, 50 F. (2d) 112. As to *Bedell v. Commissioner*, 30 F. (2d) 622, see p. 7a below. As to *Terbell v. Commissioner*, 29 B. T. A. 44, see p. 24 above.

tinguished the cases before them on their particular facts. Many of the cases cited by the Government are distinguished in *Kales v. Commissioner, supra.* If the Government had regarded the *Kales* case as in conflict with these other decisions, it would undoubtedly have applied to the Supreme Court for certiorari, but shortly after the decision of the Circuit Court of Appeals in the *Kales* case the Solicitor General announced that no such petition would be filed.

Under the Revenue Acts of 1918 and 1921 (§ 204) and the Revenue Act of 1924 (§ 206) individual taxpayers were allowed to carry forward from one year to the next net losses incurred in "business regularly carried on by the taxpayers". In applying these provisions of the statute the courts narrowed the definitions of "business" given in such cases as *Flint v. Stone Tracy Co.*, and held that everything that constituted a business did not necessarily constitute a business *regularly carried on.* Accordingly, the net loss carry-over was denied to taxpayers in a number of cases where the business consisted of occasional or isolated transactions. The Government has cited a number of these cases,[2] but obviously they are not authority for the construction of a statute which omits the word "regularly".

[2] *Bedell v. Commissioner,* 30 F. (2d) 622; *Dalton v. Bowers,* 287 U. S. 404; *Burnet v. Clark,* 287 U. S. 410; *Goldberg v. Commissioner,* 36 F. (2d) 551; *Rogers v. United States,* 41 F. (2d) 865.

APPENDIX II

APPENDIX II.

CASES ON DISTINCTION BETWEEN CAPITAL ITEMS AND EXPENSE ITEMS.

Many of the cases cited in the Government's brief denied deductions as business expense on the ground that items involved were capital items representing expenditures or investments, the benefits of which would accrue to the advantage of the taxpayer for several or many years. The tribunals held that such disbursements belonged in capital account and not in expense account. Those of them which were of a wasting nature were allowed to be recovered by way of exhaustion or depreciation over a period of years. These cases cited by the Government [1] are not applicable to carrying charges, which do not constitute an investment but merely the consideration paid for forbearance in order to postpone payment for an investment.

A number of cases are cited by the Government where a stockholder paid out money to discharge the debts or other obligations of a corporation, for the betterment of his investment in the stock. The courts held that he could not deduct these items as losses or business expense because they were not *his* losses, nor expenses of *his* business—*but they all indicated that the expenditures were in the nature of capital investments on his part,* as tending to increase the value of his stock holdings. In this they were like the

[1] *Bonwit Teller v. United States,* 53 F. (2d) 381; *Briarcliff Inv. Co. v. Commissioner,* 30 B. T. A. 1269; *Welch v. Helvering,* 290 U. S. 111; *Hutton v. Commissioner,* 39 F. (2d) 459; *Tonningsen v. Commissioner,* 61 F. (2d) 199.

Christiana stock given by Mr. du Pont to the nine executives in 1921—which he never claimed as an expense. None of the Government's authorities involved *carrying charges*, which are amounts paid out to others for the use of assets which belong in capital account.

The great fallacy in the Government's brief is that it fails to distinguish between capital items and expense items. An investment by which one acquires capital in the hope of deriving gain by way of income or increment, is a capital item,[2] even though payment therefor may be made in installments. Its cost is not deductible currently but must be recovered either over the life of the asset, through depletion, depreciation, obsolescence or exhaustion allowances, or not recovered until the asset is disposed of, when gain or loss on the purchase transaction is computed.

On the other hand, an expenditure which adds nothing to the value of the taxpayer's capital but merely enables him to use his capital or hold it for future sale, is an expense item which should be charged against annual income and which it is proper to capitalize. In this category are rent, insurance premiums, interest on borrowed capital, annual taxes and other items commonly called carrying charges. A speculator who buys a single parcel of unimproved real estate and holds it for a number of years awaiting the growth of the "unearned increment," may have to pay out during his waiting period taxes and interest in very substantial proportion to the original investment. Often he would prefer to lump these "carrying charges" in with the cost price and have them go to reduce his profit on the sale of the

[2] E. g. in *Menihan v. Commissioner*, 79 F. (2d) 305; *Cripple Creek Coal Co. v. Commissioner*, 63 F. (2d) 829; *Mastin v. Commissioner*, 28 F. (2d) 748; *Park v. Commissioner*, 58 F. (2d) 965; *Bing v. Helvering*, 76 F. (2d) 941.

land rather than deduct them annually (sometimes in years in which he had no income), but the Treasury Department has established that this is not permissible. On this point it prevailed in the case of *Westerfield v. Rafferty*, 4 F. (2d) 590, and regarded the decision of such importance that it published it as a Treasury Decision, giving it the force and effect of a Regulation (T. D. 3667, IV-1 C. B. 96).[3]

The difference between capital charges and items which go merely to maintain the *status quo*, and are thus chargeable to expense, is well exemplified in the case of coal mines. In Treasury Regulations 74, relating to the income tax under the Revenue Act of 1928, Article 242 (b) provided:

> Expenditures for plant and equipment not including expenditures for maintenance and for ordinary and necessary repairs, shall be charged to capital account recoverable through depreciation.

Coal mining companies contended that expenditures for electric locomotives, mine cars, rails, etc., made necessary to maintain output, by removal of coal and recession of working faces, should be charged to expense rather than capital because they merely served to maintain the *status quo* and did not increase output nor reduce the cost of production. The Bureau of Internal Revenue, and at first the Board of Tax Appeals,[4] held these items to be capital nevertheless.

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[3] In the Revenue Act of 1932 (subsequent to that which controls the du Pont case), Congress made a special exception for investors in "unimproved and unproductive real property" by allowing their carrying charges to be charged to capital account *if they had not been deducted in income account*. (Revenue Act of 1932, § 113 (b) (1) (A)). But even today this has not not been extended to anything except unimproved real estate.

[4] *Marsh Fork Coal Co. v. Commissioner*, 11 B. T. A. 685.

The courts took the opposite view [5] and the Board of Tax Appeals followed their decisions.[6] The Commissioner of Internal Revenue at first published non-acquiescences in the decisions of the Board, but in 1933 recognized the validity of the ruling laid down by the courts and the Board and published Treasury Decision 4376 [7] and amended the Regulation quoted above to read as follows:

> Expenditures for plant and equipment and for replacements, not including expenditures for maintenance and for ordinary and necessary repairs, shall ordinarily be charged to capital account recoverable through depreciation. Expenditures for equipment (including its installation and housing) and for replacements thereof, which are necessary to maintain the normal output solely because of the recession of the working faces of the mine, and which (1) do not increase the value of the mine, or (2) do not decrease the cost of production of mineral units, or (3) do not represent an amount expended in restoring property or in making good the exhaustion thereof for which an allowance is or has been made, shall be deducted as ordinary and necessary business expenses.

Subsequently the Board of Tax Appeals has held that this rule is not limited to mining companies but has applied

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[5] *United States v. Roden Coal Co.* (C. C. A. 5, 1930), 39 F. (2d) 425; *Marsh Fork Coal Co. v. Lucas* (C. C. A. 4, 1930), 42 F. (2d) 83; *Commissioner v. Brier Hill Collieries* (C. C. A. 6, 1931), 50 F. (2d) 777.

[6] *West Virginia-Pittsburgh Coal Co. v. Commissioner*, 24 B. T. A. 234 (1931); *Tennessee Consolidated Coal Co. v. Commissioner*, 24 B. T. A. 369 (1931); *Preston County Coke Co. v. Commissioner*, 24 B. T. A. 646 (1931); *Hutchinson Coal Co. v. Commissioner*, 24 B. T. A. 973 (1931); *Cunard Coal Co. v. Commissioner*, 26 B. T. A. 234 (1932).

[7] XII-2 C. B. 117.

it to a shoe company,[8] and has indicated that it would be applicable to a gasoline refining company under proper proof.[9]

The most recent decision of the Board of Tax Appeals at all parallel to the instant case is that in *Paul J. Bonwit v. Commissioner*, Docket No. 92548, promulgated September 5, 1939.[10] The opinion of the Board on the third issue before it was as follows:

> "The third issue presents the deductibility of the $500. annuity paid by the petitioner to Clara Philipsborn. The petitioner asserts that his trade or business was that of being chief executive of Bonwit Teller & Company of Philadelphia. With this statement of facts we agree. In *George S. Groves*, 38 B. T. A. 727 (Dec. 10,448), we said:
>
> > Even if petitioner had been but the active president of an operating corporation upon a salary, his activities would have been recognized as carrying on a trade or business within the meaning of the statute. *Ralph C. Holmes*, 37 B. T. A. 865 (Dec. 10,029) (on review, CCA 2d Cir).
>
> "So long, therefore, as the petitioner remained the president and acting head of the company he continued to be in a trade or business and was entitled to deductions for all ordinary and necessary expenses relating to that business. The record shows that he retired from the company in 1934 but does not disclose the exact date. However, the respondent makes no objection to the allowance of the deduction on that ground.

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[8] *International Shoe Co. v. Commissioner*, 38 B. T. A. 81 (1938).

[9] *Rainbow Gasoline Corp. v. Commissioner*, 31 B. T. A. 1050 (1935).

[10] A memorandum opinion published in Commerce Clearing House Board of Tax Appeals Service for 1939 at page 29,933.

"The expenditure was shown to be necessary to the company's welfare and hence to the petitioner's trade or business as its president. The facts and circumstances surrounding the agreement of the petitioner and Rosenbaum each to make an additional yearly payment to Mrs. Philipsborn do not present such an extraordinary situation as to make the statute inapplicable. See *First National Bank of Skowhegan, Maine,* 35 B. T. A. 876 (Dec. 9626); *Edward J. Miller,* 37 B. T. A. 830 (Dec. 10,024); *International Shoe Co.,* 38 B. T. A. 81 (Dec. 10,090).

"The purchase of the Philipsborn stock was obviously not a customary recurrent event, habitual to the petitioner's business but it was of such a character as might normally appear in any corporation whose stock is held by a potentially adverse interest. Likewise, the action of the petitioner and Rosenbaum, taken in order to accomplish the stock purchase, is by no means unusual. It was considered by all parties essential to the success of the move. There is no suggestion that it was prompted by any other motive than the preservation and the uninterrupted prosperity of the company's business.

"The respondent also contends that the payment was made in order to acquire capital assets. However, the company acquired the assets, not the petitioner. Later it made some distribution of them but not in proportion to the stockholdings. The petitioner obtained only a few shares. The primary purpose in purchasing the Philipsborn block of stock was to protect the company's business—and hence that of the petitioner—against its threatened acquisition by hostile interests. The deduction is allowed."

APPENDIX III.

AUTHORITIES ON MEANING OF "INTEREST."

A. Cases.

The cases are legion in which courts have defined "interest" as the compensation for the use or forbearance of a loan of money. But these cases all appear to fall into one or the other of two groups: (a) where the payment involved actually was for the loan of money, and (b) where the real question was the legislative intent in a statute against usury.

(i) *Cases where the courts were dealing with loans of money.*

In the cases in the first class, the courts used definitions sufficiently broad to cover the question before them, and cannot be presumed to have intended to decide, *obiter*, whether the word "interest" could not have a different connotation in a case where a mutuum other than a loan of money was involved.

What Mr. Justice Cardozo wrote of constitutional theory in *Snyder v. Massachusetts*, 291 U. S. 97, 114, is equally applicable to statutory construction. He said:

> A fertile source of perversion in constitutional theory is the tyranny of labels. Out of the vague precepts of the Fourteenth Amendment a court frames a rule which is general in form, though it has been wrought under the pressure of particular situations. Forthwith another situation is placed under the rule

because it is fitted to the words, though related faintly, if at all, to the reasons that brought the rule into existence.

The cases cited in the Government brief, in support of a narrow definition of interest fall, with two exceptions,[1] in the first group of cases mentioned above—where use or forbearance of money was the subject of the litigation and there was no reason for any ruling as to whether there could be "interest" on a mutuum.

Those cases are (in alphabetical order):

Baltimore & Ohio Railroad Co. v. Commissioner, 78 F. (2d) 460. The railroad company offered unissued common stock to its shareholders, ratably, at a stated price, less certain amounts if they made payment in advance of issuance of the stock. The difference was computed at six per cent per annum on the advance payments for the time between payment and delivery of the stock. The railroad company treated the difference on its books as interest accrued.

It was held that no loan and no indebtedness was involved—that the price and discount indicated were a mere formula, and no amount was deductible, in computing income taxes, as "interest on indebtedness".

Here was a mere sale of stock for future delivery—the reduction in price, even though computed at a fixed rate per annum, was not a payment in connection with any kind of a loan or of a debt.

City of Lincoln, Neb. v. Ricketts, 77 F. (2d) 425. The real question was whether money turned over by the city

[1] *Title Guaranty & Surety Co. v. Klein*, 178 Fed. 689, and *Dry Dock Bank v. American Life Ins. etc. Co.*, 3 N. Y. 344, which are usury cases discussed below, pp. 20a-21a.

to the trust company constituted a loan, as a bank deposit, or a trust fund. The contract provided for the payment of interest. Held that the provision for the payment of interest was inconsistent with the thought that the title to the money remained with the city—accordingly a loan, not a trust was involved. The definition of "interest" given by the court would have resulted in the same decision if it had read "Interest is the compensation . . . for a loan or the forbearance of a debt, regardless of whether the debt is in money or in other property repayable in kind". Nothing indicates any intent on the part of the court to hold that there could not be "interest" on a mutuum.

Corbett Investment Co. v. Helvering, 75 F. (2d) 525. Corbett bequeathed to his widow, in lieu of dower, $12,000 per annum for life out of the income and rents of real property devised to his grandsons subject to this charge. Later the widow released the estate and accepted the personal undertaking of the grandsons to pay her $1000 per month. Still later the grandsons turned the real estate over to a corporation in exchange for its capital stock and its agreement to pay $1000 per month to the widow.

Held that the payments to the widow were part of the purchase price of the property—capital items—not deductible by the corporation as interest. Nothing in this case sheds any light whatever, even by way of obiter dictum, on the problem before us.

Dry Dock Bank v. American Life Insurance etc. Co., 3 N. Y. 344. This was a usury case, discussed at p. 20a.

Fall River Electric Light Co. v. Commissioner, 23 B. T. A. 168. This case involved a question similar to that in *Old Colony Railroad Co. v. Commissioner*, 284 U. S. 552, discussed below. A loan of money was involved and a

broad construction of the income tax law was applied in favor of taxpayer. The definition of "interest" adopted was broad enough to cover the case before the Board, which had no question before it like that at bar.

Hayes v. Commissioner (Mass.) 138 N. E. 539. This case, like *New Orleans Land Co. v. Commissioner*, below, merely held that the entire purchase price of goods sold on time should be regarded as the sales price and no part of such price should be considered interest, taxable at a higher rate than profits on sale of goods. The doubt was resolved in favor of the taxpayer. This case is practically the converse of the *Baltimore & Ohio Railroad* case, *supra*.

Kishi v. Humble Oil & Refining Co., 10 F. (2d) 356. Held that defendants, having detained money, were liable for interest at statutory rate (Texas). There was no reason for an exclusive definition.

Maryland Casualty Co. v. Omaha Electric etc. Co., 157 Fed. 514. Headnote 5 reads:

> Interest is a consideration paid for the use of money, or forbearance in demanding it when due; and so long as one retains money and has its use he can make no charge against another for interest thereon.

Nothing but use of money was involved here—so there could have been no possible intent on the part of the court to make its definition of interest exclusive.

New Orleans Land Co. v. Commissioner, 29 B. T. A. 35. The sole question was whether on purchase of land part of payment was interest or it was all principal. No question of loan of something other than money is involved.

Old Colony Railroad Co. v. Commissioner, 284 U. S. 552. This case involved only a loan of money, so there was no reason for the court to pass on whether or not the

term "interest" was applicable to the consideration for loans of assets other than money. It said (p. 560):

> And as respects "interest" the *usual* import of the term is the amount which one has contracted to pay for the use of borrowed money. (Emphasis supplied.)

Naturally, the *usual* import of the term is so, because loans of money are, today, much more usual than loans of other assets to be repaid in kind. That the definition was not intended to be exclusive is clear from the fact that the court referred only to amounts *contracted* for, although interest frequently is allowed in the absence of contract, under statutes and common law decisions.

It should be particularly noted that the court, later in its opinion said (p. 561):

> If there were doubt as to the connotation of the term, and another meaning might be adopted the fact of its use in a tax statute would incline the scale to the construction most favorable to the taxpayer (citing numerous cases).

Title Guaranty & Surety Co. v. Klein, 178 Fed. 689. This was a usury case, discussed below at p. 21a.

Terbell v. Commissioner, 29 B. T. A. 44, discussed in text of brief, p. 24.

Westerfield v. Rafferty, 4 F. (2d) 590. Here there was no controversy over the meaning of "interest" and no reason for an exclusive definition. The dispute was whether "carrying charges" were currently deductible, or whether they constituted capital items. Cf. pp. 9a-10a above.

The District Court in its opinion (R. 241) cited certain other cases on the definition of "interest" which are not

cited in the Government's brief in this court. All of them are in the same category as the cases analyzed above. The courts were dealing with money indebtedness, and, in giving definitions of "interest", had no reason to consider whether that term was applicable in the case of a mutuum. The cases are:

Redfield v. Ystalyfera Iron Co., 110 U. S. 174. This case involved the right to interest on a judgment. The court held that where interest is given as damages it may be withheld if plaintiff has been guilty of laches. This makes it clear that the concept of "interest" can be broader than mere compensation for the use of money. The opinion contains no definition of "interest".

Loudon v. Taxing District of Shelby County, 104 U. S. 771. The plaintiff had been compelled to borrow money to carry out its contract and demanded that the defendant, in addition to the contract price and legal interest, reimburse it for the difference between the legal interest on the contract price and the interest plaintiff had paid out. The court held

> all damages for delay in the payment of money owing upon contract are provided for in the allowance of interest, which is in the nature of damages for withholding money that is due.

This patently is not an exhaustive definition—it does not even cover interest on a loan of money that is not due.

Appeal of Bettendorf, 3 B. T. A. 378. The Board held that interest allowed as damages—as in *Redfield v. Ystalyfera Iron Co., supra*—was not deductible as "interest on indebtedness". The Board was not considering whether there could be interest on a mutuum.

(ii) *Usury cases.*

The second class of cases referred to above as containing definitions of "interest" are those involving the usury statutes where forfeitures or penalties are imposed upon persons charging excessive amounts for forbearance of loans. Since usury statutes are in derogation of the common right and are in word or effect penal statutes, they are construed strictly against those who invoke their provisions. The leading case is *Dry Dock Bank v. American Life Insurance & Trust Co.*, 3 N. Y. 344 (1850). It involved the New York statute against usury which prohibited excessive interest for the loan or forbearance of money, goods or things in action. By a complicated deal in foreign exchange (subject however to agreement that the pound Sterling should be regarded as equivalent to $5.00), three banking institutions arranged what was in effect a loan of money. The court held that because it was in effect a loan of money the usury law applied. The court said (p. 355):

> The terms "interest" and "forbearance" cannot be predicated of any other than a loan of money, actual or presumed. Interest is defined to be a *certain profit* for the use of the loan; and forbearance the giving of a further day, when the time originally limited for the return of the loan, has passed. Both imply that the thing loaned has an established value, so that the lender on its return, with the compensation fixed by law for the use and risk, may receive a "certain profit". Now this is true only of money, which is legally supposed to have a fixed, unchangeable value in itself, and to be consequently the true measure of the value of all other property. A fixed rate per cent on money, therefore, in contemplation of law, is supposed to give the lender a "certain profit", because the thing loaned is of the

same value at the end of the term as at its commencement.

It may be very good logic to hold that the terms "interest" and "forbearance" *in a usury statute* cannot be predicated of any other than a loan of money for the reasons given in the quotation above. But this does not mean that the word "interest" in a *tax* statute is restricted to that narrow limit.

At page 354 the court said:

> The statute of Henry VIII enumerated, and prohibited, the various devices and expedients adopted by money lenders, to evade the previous laws against usury. The statute of 12 Ann. from which our own is substantially taken, followed the earlier legislation upon this subject, by a partial enumeration of these devices; while that statute, like our own, contains a general prohibition against taking, or securing, more than the legal rate of interest, *directly* or *indirectly*, for the loan or forbearance of any money, which rendered such enumeration unnecessary.

And at page 355 added:

> The true construction of the last two statutes, as I apprehend, is, and has been, that no more than the prescribed rate of interest should be taken, on a loan, or forbearance of money, *directly* or *indirectly*, by way of loan of goods, or choses in action, or in any other manner.

We submit that the logic of the court shown in the first quotation given above is probably sounder than its history reflected in the second and third quotations, and we refer this Court to the old English statutes which are reproduced below, at pp. 24a-35a.

The Government's brief also cites *Title Guaranty & Surety Co. v. Klein*, 178 Fed. 689, which was another case

involving the New York usury law. Without citing them by name, the court relied on the New York decisions which began with the *Dry Dock Bank* case, *supra*. This decision is only authority for the interpretation of usury laws and not for the meaning of "interest" when found elsewhere.

B. Statutes.

Statutes Shedding Light on Meaning of "Interest."

The Code of the District of Columbia, Title 17, Chapter 1, Section 1:

> Rate of interest in absence of agreement.—The rate of interest in the District upon the loan or forbearance of any money, goods, or things in action, and the rate to be allowed in judgments and decrees, in the absence of express contract as to such rate of interest, shall be six dollars upon one hundred dollars for one year, and at that rate for a greater or less sum or for a longer or shorter time: *Provided*, That interest, when authorized by law, on judgments against the District of Columbia, shall be at the rate of not exceeding 4 per centum per annum. (Sept. 30, 1890, 26 Stat. 514, c. 1126; Mar. 3, 1901, 31 Stat. 1377; c. 854, sec. 1178; July 1, 1902, 32 Stat. 610, c. 1352.)

Similar statutes in the states fixing the legal rate of interest "upon the loan or forbearance of money, goods or things in action" are:

Alabama. Code of 1928, Chapter 308, Section 8563.
California. Act approved at General Election of November 5, 1918. Stats. 1919 lxxxiii (General Laws of California, 1923, p. 1384).
Colorado. Compiled laws, 1921, Section 3781.
Connecticut. Revised Statutes of 1930, Section 4066.
Hawaii. Revised Laws, Section 7055.

Illinois. Cahill's Illinois Revised Statutes, Chapter 74, Section 1.

Indiana. Burns Indiana Statutes, Chapter 19, Section 2004.

Maine. Revised Statutes, Chapter 57, Section 143.

Minnesota. Mason's Minnesota Statutes, Section 7036.

Nebraska. Compiled Statutes, 1929, Chapter 45, Sections 101, 102.

New Hampshire. Public Laws, 1926, Chapter 269, Section 15.

New Mexico. Annotated Statutes, 1929, Chapter 89, Section 109.

New York. General Business Law, Section 370.

North Dakota. Compiled Laws, 1913, Section 6073.

Utah. Revised Statutes, 1933, Title 44, Section 44-0-1.

Washington. Remington's Compiled Statutes, 1922, Section 7299.

Wisconsin. Wisconsin Statutes, 1935, Section 115.04.

Wyoming. Revised Statutes, 1931, Chapter 58, Section 101.

Other statutes substituting equivalent words for "money, goods or things in action", are:

Iowa. Code of Iowa Annotated, Title 23, Chapter 418:
for the loan of money, or upon contract founded upon any sale or loan of real or personal property.

Kentucky. Carroll's Kentucky Statutes, Chapter 72, Section 2219:
loan or forbearance of money, or other thing of value.

Missouri. Revised Statutes, 1929, Section 4842:
loan of money or other commodity.

New Jersey. Compiled Statutes, p. 5704, Section 1:
loan of any money, wares, merchandise, goods and chattels.

South Carolina. Code of Laws, 1932, Section 6738:
any contract arising in this state for the hiring, lending or use of money or other commodity.

Virginia. Code of 1924, Section 5551:
loan or forbearance of money or other thing.
West Virginia. Barnes West Virginia Code Annotated, 1923, Chapter 96, Section 5:
loan or forbearance of money or other thing.

British Statutes Against Usury in Force at Various Times Prior to the General Repeal of the Usury Laws in 1854.

37 Henry VIII, c. IX (1545).

A Bill Against Usury.

'Where before this Time divers and sundry Acts, Statutes and Laws have been ordained, had and made within this Realm, for the avoiding and Punishment of Usury, being a Thing unlawful, and of other corrupt Bargains, Shifts and Chevisances, (2) which Acts, Statutes and Laws been so obscure and dark in Sentences, Words and Terms, and upon the same so many Doubts, Ambiguities and Questions have risen and grown, and the same Acts, Statutes and Laws been of so little Force or Effect, that by reason thereof little or no Punishment hath ensued to the Offenders of the same, but rather hath encouraged them to use the same:' (3) For Reformation whereof, be it enacted by the King our Sovereign Lord, by the Assent of the Lords Spiritual and Temporal, and of the Commons, in this present Parliament assembled, and by the Authority of the same, That all and every the said Acts, Statutes and Laws heretofore made, of, for or concerning Usury, Shifts, corrupt Bargains and Chevisances, and every of them, and all Pains, Forfeitures and Penalties concerning the same, and every Part thereof, shall from henceforth be utterly void and of none Effect, to all Intents, Constructions and Purposes.

II. And be it further enacted by the Authority aforesaid, That no Person or Persons of what Estate, Degree or Condition soever he or they be, from and after the last Day of January next coming, shall by himself, Factor, Attorney, Servant or Deputy, sell his Merchandises or Wares to any Person or Persons, and within three Months next after, by himself, Factor, Attorney, Deputy, or by any other Person or Persons to his Use and Behoof, buy the same Merchandises or Wares, or any Part or Parcel thereof, upon a lower price, knowing them to be the same Wares or Merchandises that he before did so bargain and sell, upon the Pains and Forfeitures hereafter limited in this Estatute.[1]

III. And be it also enacted by the same Authority, That no Person or Persons, of what Estate, Degree, Quality or Condition soever he or they be, at any Time after the said last Day of January next coming, by Way or Mean of any corrupt Bargain, Loan, Eschange, Chevisance, Shift, Interest of any Wares, Merchandises, or other Thing or Things whatsoever, or by any other corrupt or deceitful Way or Mean, or by any Covin, Engin or deceitful Way or Conveyance, shall have, receive, accept or take in Lucre or Gains for the forbearing or giving Day of Payment of one whole

[1] When a borrower goes to a lender and goes through the form of selling a chattel to the lender and taking an option for its repurchase at a higher price, this is obviously a device equivalent to the lending of money on pawn at interest, but it should be noted that Section 2 of the Statute of Henry VIII was aimed at the converse of this, where goods were loaned through the device of a sale and the lender repurchased them at a lower price, so that in effect it was the borrower of the goods, not the borrower of the money, who paid the premium for the loan; and the statute was aimed at this as much as at the converse device where the borrower of the money had to pay.

Year of and for his or their Money or other Things that shall be due for the same Wares, Merchandises, or other Thing or Things, above the Sum of ten Pound in the Hundred, and so after that Rate, and not above, of and for a more or less Sum, or for a longer or shorter Time, and no more or greater Gain or Sum thereupon to be had, upon the Pains and Forfeitures hereafter in this Act mentioned and contained.

IV. And be it further enacted by the Authority aforesaid, That if any Person or Persons, at any Time after the said last Day of January, do bargain and sell, or lay to Mortgage by any Way or Mean, any Manors, Lands, Tenements or Hereditaments, to any Person or Persons, upon Condition of payment or Non-payment of any Sum or Sums of Money to be had, paid or made at any Day certain, or before any such Day by him that shall so bargain, sell or lay to Mortgage the same Manors, Lands, Tenements or Hereditaments, that the same Person or Persons, to whom any such Manors, Lands, Tenements or Hereditaments shall be so bargained, sold or laid to mortgage, shall not by reason thereof have, ne take, in Lucre or Gains of the Issues, Revenues and Profits of the same Manors, Lands, Tenements, or Hereditaments, above the Sum of ten Pound in the Hundred for one whole Year, and so after the Rate above-paid for a more or lesser Sum, or for a longer or shorter Time, and no more, nor otherwise, upon the Pains, Forfeitures and Penalties hereafter in this present Estatute limited and expressed.

V. And be it further enacted by the Authority aforesaid, That if any Person or Persons, of what Estate, Degree, Quality or Condition soever he or they be, at any Time after the said last Day of January next coming, shall do any

Act or Acts, Thing or Things, contrary to the Tenor, Form and Effect of this Estatute, or of any Clause, Article or Sentence contained in the same, that then all and every Offender and Offenders therein, or in any Part thereof, shall forfeit and lose for every such Offence the treble Value of the Wares, Merchandises, and other Thing or Things so bargained, sold, exchanged or shifted, (2) and the treble Value of the Issues and Profits of the said Manors, Lands, Tenements and Hereditaments so had, taken or received by reason of any such Bargain, Sale or Mortgage, (3) and also shall have and suffer Imprisonment of his Body, and make Fine and Ransom at the King's Will and Pleasure; (4) the Moiety of which Forfeiture of the said treble Value shall be to the King, and the other Moiety to him or them that will sue for the same in any of the King's Courts, by Action of Debt, Bill, Plaint or Information, in which Action, Bill, Plaint or Information, no Wager of Law, Essoin or Protection shall be admitted or allowed.

VI. Provided alway, and be it enacted by the Authority aforesaid, That this Act, or any Thing therein contained, shall not in any wise extend to any lawful Obligation indorsed with a Condition, nor to any Statute or Recognizance made and to be made for the Payment of a lesser Sum, so that the same Obligation, Statute or Recognizance be made for a true, just and perfect Debt, or for the performance of any other true Covenants, made or to be made upon a just and true Intent had between the Parties, other than in Cases of Usury, Interest, corrupt Bargains, Shift or Chevisance; (2) ne yet shall extend to any Recovery, Fine Feoffment, Release, Confirmation or Grant made or to be made upon Condition with a true Intent, other than to such Recoveries, Fines, Feoffments, Releases, Confirmations and

Grants, as shall be made upon Condition extending to Usury, Interest, corrupt Bargains, Shifts or Chevisance; any Thing in this Statute contained, or any Law, Statute or Ordinance heretofore had, used or made to the contrary notwithstanding.

21 James I, c. XVII. (1623)

An Act against Usury.

'WHEREAS at this Time there is a very great Abatement in the Value of Land, and other the Merchandizes, Wares and Commodities of this Kingdom, both at Home, and also in foreign Parts whither they are transported;' (2) and whereas divers Subjects of this Kingdom, as well the Gentry as Merchants, Farmers and Tradesmen, both for their urgent and necessary Occasions for the following their Trades, Maintenance of their Stocks and Employments, have borrowed, and do borrow divers Sums of Money, Wares, Merchandizes and other Commodities; (3) but by reason of the said general Fall and Abatement of the Value of Land, and the Prices of the said Merchandize, Wares and Commodities, and Interest in Loan continuing at so high a Rate as ten Pounds in the hundred Pounds for a Year, doth not only make Men unable to pay their Debts, and continue the Maintenance of Trade, but their Debts daily increasing, they are enforced to sell their Lands and Stocks at very low Rates, to forsake the Use of Merchandize and Trade, and to give over their Leases and Farms, and so become unprofitable Members of the Commonwealth, to the great Hurt and Hinderance of the same:'

II. Be it therefore enacted by the King's most excellent Majesty, the Lords Spiritual and Temporal, and the Commons, in this present Parliament assembled, That no

Person or Persons whatsoever, from and after the four and twentieth Day of June, which shall be in the Year of our Lord one thousand six hundred twenty and five, upon any Contract to be made after the said four and twentieth Day of June, shall take directly or indirectly, for Loan of any Monies, Wares, Merchandize or other Commodities whatsoever, above the Value of eight Pounds for the Forbearance of one hundred Pounds for a Year, and so after that Rate for a greater or lesser Sum, or for a longer or shorter Time; (2) and that all Bonds, Contracts and Assurances whatsoever made after the Time aforesaid, for Payment of any Principal or Money to be lent or covenanted to be performed, upon or for any Usury, whereupon or whereby there shall be reserved or taken above the Rate of eight Pounds in the hundred as aforesaid, shall be utterly void; (3) and that all and every Person and Persons whatsoever, which shall after the Time aforesaid, upon any Contract to be made after the said four and twentieth Day of June, which shall be in the Year of our Lord 1625, take, accept and receive, by Way or Means of any corrupt Bargain, Loan, Exchange, Chevisance, Shift or Interest of any Wares, Merchandize or other Thing or Things whatsoever, or by any deceitful Way or Means, or by any Covin, Engine or deceitful Conveyance, for the forbearing or giving Day of Payment for one whole Year, of and for their Money or other Thing, above the Sum of eight Pounds for the forbearing of one hundred Pounds for a Year, and so after that Rate for a lesser or greater Sum, or for a longer or shorter Time, shall forfeit and lose for every such Offence the treble Value of the Monies, Wares, Merchandizes and other Things so lent, bargained, sold, exchanged or shifted.

III. And be it further enacted by the Authority aforesaid, That all and every Scrivener and Scriveners, Broker

and Brokers, Solicitor and Solicitors, Driver and Drivers of Bargains for Contracts, who shall after the said twenty-fourth Day of June, which shall be in the Year of our Lord 1625, take or receive, directly or indirectly, any Sum or Sums of Money, or other Reward or Thing for Brocage, soliciting, driving or procuring the Loan or forbearing of any Sum or Sums of Money, over or above the Rate or Value of five Shillings for the Loan or forbearing of one hundred Pounds for a Year, and so ratably, or above twelve Pence for making or renewing of the Bond or Bill for the Loan, or forbearing thereof, or for any Counter Bond or Bill concerning the same, shall forfeit for every such Offence twenty Pounds, and have Imprisonment for Half a Year; (2) the one Moiety of all which Forfeitures to be to the King our Sovereign Lord, his Heirs and Successors, and the other Moiety to him or them that will sue for the same in the same County where the several Offences are committed, and not elsewhere, by Action of Debt, Bill, Plaint or Information, in which no Essoin, Wager of Law or Protection to be allowed.

IV. This Act to continue for the Space of seven Years from the said four and twentieth Day of June, which shall be in the Year of our Lord 1625, and so to the End of the first Session of Parliament then next following.

V. Provided, That no Words in this Law contained shall be construed or expounded to allow the Practice of Usury in point of Religion or Conscience. [Made perpetual by 3 Car. 1. c. 4. §. 5. 2 H. 3. c. 5. 3 H. 7. c. 6. 11 H. 7. c. 8. 37 H. 8. c. 9. 5 & 6 Ed. 6. c. 20. 13 El. c. 8.]

12 Charles II, c. XIII.

An Act for the restraining the taking of excessive Usury.

'Forasmuch as the Abatement of Interest from Ten in the Hundred in former Times hath been found by notable Experience beneficial to the Advancement of Trade and Improvement of Lands by good Husbandry, with many other considerable Advantages to this Nation, especially the reducing of it to a nearer Proportion with Foreign States with whom we traffick: (2) And whereas in fresh Memory the like Fall from Eight to Six in the Hundred, by a late constant Practice hath found the like Success, to the general Contentment of this Nation, as is visible by several Improvements. (3) And whereas it is the Endeavour of some at present to reduce it back again in Practice to the Allowance of the Statute still in Force, to Eight in the Hundred, to the great Discouragement of Ingenuity and Industry in the Husbandry, Trade and Commerce of this Nation:'

II. Be it, for the Reasons aforesaid, enacted by the King's most Excellent Majesty, and the Lords and Commons in this present Parliament assembled, That no Person or Persons whatsoever, from and after the twenty-ninth Day of September in the Year of our Lord one thousand six hundred and sixty, upon any Contract, shall from and after the said twenty-ninth of September take directly or indirectly for Loan of any Monies, Wares, Merchandize or other Commodities whatsoever, above the Value of six Pounds for the Forbearance of one hundred Pounds for a Year, and so after that Rate for a greater or lesser Sum, or for a longer or shorter Time: (2) And that all Bonds, Contracts and Assurances whatsoever, made after the Time aforesaid for Payment of any Principal or Money to be lent, or covenanted to be performed, upon or for any Usury,

whereupon or whereby there shall be reserved or taken above the Rate of six Pounds in the Hundred, as aforesaid, shall be utterly void: (3) And that all and every Person or Persons whatsoever, which shall after the Time aforesaid, upon any Contract to be made after the said twenty-ninth Day of September, take, accept and receive, by Way or Means of any corrupt Bargain, Loan, Exchange, Chevisance, Shift, or Interest of any Wares, Merchandize, or other Thing or Things whatsoever, or by any deceitful Way or Means, or by any Covin, Engine or deceitful Conveyance, for the forbearing or giving Day of Payment for one whole Year, of and for their Money or other Thing, above the Sum of six Pounds for the forbearing of one hundred Pounds for a Year, and so after that Rate for a greater or lesser Sum, or for a longer or shorter Term, shall forfeit and lose for every such Offence the treble Value of the Monies, Wares, Merchandize and other Things so lent, bargained, sold, exchanged or shifted.

III. And be it further enacted by the Authority aforesaid, That all and every Scrivener and Scriveners, Broker and Brokers, Solicitor and Solicitors, Driver and Drivers of Bargains for Contracts, who shall after the said twenty-ninth Day of September take or receive directly or indirectly any Sum of Sums of Money, or other Reward or Thing, for Brokage, Soliciting, Driving or procuring the Loan, or forbearing of any Sum or Sums of Money, over and above the Rate or Value of five Shillings for the Loan or Forbearing of one hundred Pounds for a Year, and so rateably, or above twelve-pence for the making or renewing of the Bond or Bill for Loan, or for forbearing thereof, or for any Counterbond or Bill concerning the same, shall forfeit for every such Offence twenty Pounds, and have

Imprisonment for half a Year; (2) the one moiety of all which Forfeitures to be to the King our Sovereign Lord, his Heirs and Successors; and the other Moiety to him or them that will sue for the same in the same County where the several Offences are committed, and not elsewhere, by Action of Debt, Bill, Plaint or Information; in which no Essoin, Wager of Law or Protection to be allowed.

12 Ann., Stat. II, c. 16 (1713)

An Act to reduce the Rate of Interest, without any Prejudice to Parliamentary Securities.

Whereas the Reducing of Interest to ten, and from thence to eight, and thence to six in the Hundred, hath, from Time to Time, by Experience been found very beneficial to the Advancement of Trade, and Improvement of Lands: And whereas the heavy Burden of the late long and expensive War hath been chiefly born by the Owners of the Land of this Kingdom, by Reason whereof they have been necessitated to contract very large Debts, and thereby, and by the Abatement in the Value of their Lands, are become greatly impoverished: And whereas by Reason of the great Interest and Profit which hath been made of Money at Home, the Foreign Trade of this Nation hath of late Years been much neglected, and at this Time there is a great Abatement in the Value of the Merchandizes, Wares, and Commodities of this Kingdom, both at Home and in Foreign Parts, whither they are transported: And whereas for the Redress of these Mischiefs, and the preventing the Increase of the same, it is absolutely necessary to reduce the high Rate of Interest of six Pounds in the hundred Pounds for a Year to a nearer proportion with the Interest allowed for Money in Foreign States:

Be it therefore enacted by . . . That no Person or Persons whatsoever, from and after the nine and twentieth Day of *September* in the Year of our Lord one thousand seven hundred and fourteen, upon any Contract, which shall be made from and after the said nine and twentieth Day of *September*, take, directly or indirectly, for Loan of any Monies, Wares, Merchandize, or other Commodities whatsoever, above the Value of five Pounds for the Forbearance of one hundred Pounds for a Year, and so after that rate for a greater or lesser Sum, or for a longer or shorter Time; and that all Bonds, Contracts, and Assurances whatsoever, made after the Time aforesaid, for Payment of any Principal, or Money to be lent or covenanted to be performed upon or for any Usury, whereupon or whereby there shall be reserved or taken above the Rate of five Pounds in the Hundred, as aforesaid, shall be utterly void; and that all and every Person or Persons whatsoever, which shall after the Time aforesaid, upon any Contract to be made after the said nine and twentieth Day of *September*, take, accept and receive, by Way or Means of any corrupt Bargain, Loan, Exchange, Chevizance, Shift or Interest of any Wares, Merchandize, or other Thing or Things whatsoever, or by any deceitful Way or Means, or by any Covin, Engine, or deceitful Conveyance, for the forbearing or giving Day of Payment for one Whole Year, of and for their Money or other Thing, above the Sum of five Pounds for the forbearing of one hundred Pounds for a Year, and so after that a Rate for a greater or lesser Sum, or for a longer or shorter Term, shall forfeit and lose for every such Offence the treble Value of the Monies, Wares, Merchandizes, and other Things so lent, bargained, exchanged or shifted.

I. And be it further enacted by the Authority aforesaid, That all and every Scrivener and Scriveners, Broker

and Brokers, Solicitor and Solicitors, Driver and Drivers of Bargains for Contracts who shall after the said nine and twentieth Day of *September* take or receive, directly or indirectly, any Sum or Sums of Money, or other Reward or Thing for Brokage, soliciting, driving, or procuring the Loan, or forbearing of any Sum or Sums of Money, over and above the Rate or Value of five Shillings for the Loan, or forbearing of one hundred Pounds for a Year, and so ratably, or above twelve Pence, over and above the Stamp-Duties, for making or renewing the Bond or Bill for Loan, or forbeating thereof, or for any Counterbond or Bill concerning the same, shall forfeit for every such Offence twenty Pounds, with Costs of Suit, and suffer Imprisonment for Half a Year; the one Moiety of all which Forfeitures to be to the Queen's most Excellent Majesty, her Heirs and Successors, and the other Moiety to him or them that will sue for the same in the same County where the several Offences are committed, and not elsewhere, by Action of Debt, Bill, Plaint or Information, in which no Essoin, Wager of Law, or Protection shall be allowed.

C. The Economists.

SIR DUDLEY NORTH

Discourses upon Trade; principally directed to the Cases of the Interest, Coynage, Clipping, and Increase of Money. London 1691. [In the *Early English Tracts on Commerce*, ed. MacCulloch, London, 1856, p. 517.]

"Now as there are more Men to Till the Ground than have Land to Till, so also there will be many who want Stock to manage; and also (when a Nation is grown rich) there will be Stock for Trade in many hands, who either have not the skill or care not for the trouble of managing it in Trade. But as the Landed Man letts his Land, so these still lett their Stock; this latter is call'd Interest, but is only Rent for Stock, as the other is for Land."

A. R. J. TURGOT

Sur la Formation et la Distribution des Richesses (1766) [Œuvres de Turgot, Paris 1844].

§ 78. "Au marché, une mesure de blé se balance avec un certain poids d'argent; c'est une quantité d'argent qu'on achète avec la denrée; c'est cette quantité qu'on apprécie et qu'on compare avec d'autres valeurs étrangères.—Dans le prêt a l'intérêt, l'objet de l'appréciation est l'usage d'une certaine quantité de valeurs pendant un certain temps. Ce n'est plus une masse d'argent qu'on compare à une masse de blé; c'est une masse de valeurs qu'on compare avec une portion déterminée d'elle-même, qui devient le prix de l'usage de cette masse pendant un certain temps."

ADAM SMITH

Wealth of Nations (1776), II., 4.

"As the quantity of stock to be lent at interest increases, the interest, or the price which must be paid for the use of that stock, necessarily diminishes. . . .

"Almost all loans at interest are made in money, either of paper, or of gold and silver; but what the borrower really wants, and what the lender really supplies him with, is not the money, but the money's worth, or the goods which it can purchase . . . By means of the loan, the lender, as it were, assigns to the borrower his right to a certain portion of the annual produce of the land and labour of the country, to be employed as the borrower pleases. The quantity of stock, therefore, or, as it is commonly expressed, of money which can be lent at interest in any country, is not regulated by the value of the money, whether paper or coin, which serves as the instrument of the different loans made in that country" [ibid. II. 4].

J. B. SAY

Traité d'Economie Politique. (1803). 1841 Ed. (Paris).

"L'intérêt des capitaux prêtés, mal à propos nommé *intérêt de l'argent,* s'appelait auparavant *usure* (loyer de l'usage, de la jouissance), et c'etait le mot propre, puisque l'intérêt est un prix, un loyer qu'on paie pour avoir la jouissance d'une valeur." [p. 384].

"Ce qu'on prête est une valeur accumulée et consacrée à un placement." [p. 394.]

G. CASSEL

The Nature and Necessity of Interest. (Macmillan, 1903), p. 4.

"The lender had a right to compensation for any loss which he could prove that he had suffered in consequence of the loan. This compensation is the original meaning of our modern term '*interest.*' The right to compensation for the '*damnum emergens*' was first recognised; afterwards also that for the '*lucrum cessans.*' Nothing could be better calculated to establish the common nature of the interest on a person's own trade-capital and on the money he lent to other persons, than this right to compensation for a gain which the lender would have been able to make, had he not lent his money. This became still more evident when, as in Genoa, the opportunity of discounting bills was generally recognised as a ground for claiming the *lucrum cessans.* Thus 'interest' more and more became the general term given to payments for business-loans, whilst 'usury' was restricted to signify the payment for money-advances made for consumption."

CHARLES J. BULLOCK

Elements of Economics, 2d Edition (Silver Burdette & Co. 1913), p. 261.

"Since money is the medium by which most transfers of capital are made, and the standard by which its value is measured, an investment of capital is often called an investment of money, and interest is frequently said to be a payment for the use of money. Such a choice of terms does no harm if one is careful to remember that in most cases it is other things than money that are actually invested; and that interest is paid for productive capital, whatever its form may be."

F. W. TAUSSIG

Principles of Economics (Macmillan & Co. 1915).

Taussig points out (Vol. ii, pp. 30-31) that in early days, and today in non-commercial communities, most money lending was at high rates to the improvident or necessitous—usually persons in immediate need, timid, ignorant and anxious for privacy. Under these circumstances, the rates charged were not likely to be competitive. These were loans for consumption. He contrasts them with loans for production, saying (at p. 33 of Vol. ii):

> "The tenant normally pays as rental a sum sufficient to reimburse the owner or landlord for repairs, depreciation, and such charges as insurance and taxes; and he pays him in addition a sum which constitutes a net income to the landlord, and which is the interest on his investment. . . .
>
> "A postponement of satisfactions on the landlord's part is necessarily involved, and will not be accepted unless there is some inducement,—unless the tenant pays *more* than enough to repay the sum originally invested; that is unless interest is paid."

At p. 35:

> "Pianos, the furniture in lodgings. . . . In these, wear and tear, and allowance for depreciation, play a larger part than in dwellings, and interest forms a smaller proportion of the gross rental."

At p. 36:

> "The most general statement of the conditions under which interest arises is that it results from an exchange for things future."

At p. 37:

> "§ 5. When once the payment of interest is a familiar and accepted fact, it is extended to all cases where present means are in one person's hand and are turned over to another person."

THOMAS N. CARVER

Principles of Political Economy (Ginn & Co. 1919), p. 436.

"*Interest a part of the general law of value and price.* The price which is paid for the use of capital comes under the same law as the price which is paid for anything else."

E. R. A. SELIGMAN

Principles of Economics (Longmans Green & Co. 1923), p. 219.

"Yet the word 'interest' itself means difference. *Interesse* in Latin was the sum that lay between (*inter*) the original loan and its return. . . .

"Interest, in other words, is a discount, or difference between the present and future. . . . interest is the difference in value of a present over a future enjoyment."

At p. 395:

"To the ordinary man interest seems to be the payment for a loan of money, precisely as wealth seems to consist of a sum of money. In point of fact, however, interest is paid for the use of the capital which the money represents."

See particularly discussion on pp. 398-401.

At p. 533:

"The general interest rate is, as we know, the payment for the use of capital as a whole. The 'money rate' or 'discount rate' in the long run follows the general rate of interest, for a relative plethora or dearth of capital ultimately finds its way to the lending centres."

L. M. FRASER

Economic Thought and Language—A Critique of Fundamental Economic Concepts (Macmillan & Co. 1937).

Fraser does not give a definition of interest but it is notable that he classifies productive rsources in four classes and names their products as follows:

(1)	Land	Rent
(2)	Labor	Wages
(3)	Capital	Interest
(4)	Enterprise	Profit

Apparently, irredeemable bonds are issued by British railroads just as consols are issued by the government. Fraser suggests (p. 279)—Suppose a farmer transfers land to the railroad company in exchange for irredeemable bonds. No *money* being loaned none to be repaid (except the interest). It is pointed out that he is in no different situation from the next farmer who turns his land over to the railroad under a perpetual lease and receives rent in perpetuity.

From the viewpoint of the economists, classifying income in the way Fraser does there would be no difference between interest on corporate bonds and dividends on corporate stock except that in the latter the rate of return and the principal amount recoverable are contingent. It may well be that Congress recognized that the term "interest" could be broad enough, if used alone, to include dividends on stock, and therefore it was careful, in providing for deductions from gross income, to limit the deductible interest to *interest on indebtedness.*

SUPREME COURT OF THE UNITED STATES.

No. 151.—October Term, 1939.

Pearl E. Deputy and the Sussex Trust Co., a Corporation of the State of Delaware, as Administratrix and Administrator of the Estate of Willard P. Deputy, Deceased, Late Collector of Internal Revenue, Petitioner,
vs.
Pierre S. du Pont.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[January 8, 1940.]

Mr. Justice Douglas delivered the opinion of the Court.

This case presents the question of whether respondent in computing his taxable net income for the year 1931 may deduct payments of $647,711.56 made by him in that year to the Delaware Realty and Investment Co. (hereinafter called the Delaware Company). The deduction is sought either under § 23(a) of the Revenue Act of 1928 (45 Stat. 791) as "ordinary and necessary expenses paid or incurred during the taxable year in carrying on" the "trade or business" of respondent; or under § 23(b) as "interest paid or accrued within the taxable year on indebtedness." The Commissioner disallowed the deduction and determined a deficiency, which respondent paid and now seeks to recover. It is agreed that if the deduction is allowed, respondent is entitled to judgment for $172,351.64. The judgment of the District Court against respondent (22 F. Supp. 589) was reversed by the Circuit Court of Appeals (103 F. (2d) 257). We granted certiorari because of the asserted inconsistency of that ruling with *Welch* v. *Helvering*, 290 U. S. 111, which construed the meaning of the words "ordinary and necessary expenses"; and with *Burnet* v. *Clark*, 287 U. S. 410, which limited such deductions to losses directly connected with the taxpayer's business.

Respondent's claim to the deduction arose out of the following transactions, briefly summarized. Respondent was beneficial owner of about 16% of the stock of E. I. du Pont de Nemours and Com-

pany (hereinafter called the du Pont Company). In 1919 the du Pont Company constituted a new executive committee composed of nine young men. For business reasons, it thought it desirable that these men have a financial interest in the company. Alleged legal difficulties stood in the way of the du Pont Company selling them the 9,000 shares desired.[1] Accordingly, respondent undertook to sell them 1,000 shares each. But since he did not have readily available that amount from his own holdings,[2] he borrowed 9,000 shares of the du Pont Company from Christiana Securities Company,[3] under an agreement whereby he agreed to return the stock loaned in kind within ten years and in the interim to pay to the lender all dividends declared and paid on the shares so loaned.[4] Respondent thereupon sold the shares to the nine executives, the purchase price being furnished by the du Pont Company.[5] In October, 1929 when

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[1] As stated by the District Court, counsel advised that the du Pont Company could issue stock only for money paid, labor performed, or real or personal property acquired; and that if the stock were to be issued for cash, it must first be offered to existing stockholders. According to the findings the du Pont Company did not have 9,000 shares of its stock, other than unissued stock; that stock was not then listed on the New York Stock Exchange; and the over-the-counter market was quite inactive. Nine thousand shares could not have been purchased on this market without substantially raising the price per share.

[2] Respondent had available only seventy four shares. He had a reversionary interest in two trusts which held 24,000 shares. And he was the owner of 29,125 shares of common stock of Christiana Securities Company out of a total of 75,000 shares issued and outstanding. That company was then the owner of 183,000 shares of common stock of the du Pont Company out of a total of 588,542 shares issued and outstanding.

[3] *Supra*, note 2.

[4] As security respondent gave Christiana Securities Company 3,800 shares of its capital stock. All dividends on that stock were to be paid to respondent.

[5] These sales were made at the price of $320 a share, that being approximately their book value. The du Pont Company loaned to each of the nine executives the necessary funds to purchase his 1,000 shares. They paid respondent $2,880,000 in cash for the 9,000 shares. According to respondent's brief, he turned over this sum through transactions in General Motors stock which ultimately yielded him a great profit. See du Pont v. Commissioner, 37 B. T. A. 1198.

By March 1921, the stock of the du Pont Company had declined in value and the bargain made by the executives had become a disadvantageous one. Respondent thereupon offered to turn over 400 shares of the Christiana Securities Company (of a net value of $160,000) to be held by the du Pont Company as additional collateral on the loan made to these executives, respondent to have the right to redeem those 400 shares by payment of $160,000 on maturity of the loan, that payment, if made, to be applied to the loan. If respondent failed to redeem those shares, they were to become the property of the executives on payment of their loans. Meanwhile dividends on the 400 shares up to $8,000 per annum were to go to the executives, the balance to respondent, who was, however, to return his portion to the executives if he did not redeem the

the ten-year period was about to expire, respondent did not have available the number of shares which he was obligated to return to Christiana Securities Company.[6] Therefore, he arranged for a loan from the Delaware Company of the number of shares necessary to discharge that obligation.[7] Under a contract with that company, respondent agreed to return in kind the number of shares loaned (plus any increase by stock dividend or otherwise) within ten years; to pay to the Delaware Company an amount equivalent to all dividends declared and paid on the borrowed shares until returned; and to reimburse the Delaware Company for all taxes accruing against it by reason of the agreement.

Pursuant to that agreement respondent paid the Delaware Company in 1931, the sum of $567,648, being an amount equivalent to the dividends received by him during that period from the du Pont Company on the borrowed shares; and the sum of $80,063.56, being the amount of the federal income tax imposed upon the lender by reason of the foregoing payments which it had received from respondent. These are the expenditures claimed as a deduction in the present suit.

The District Court concluded, on the basis of respondent's large and diversified investment holdings and his wide financial and business interests, that his business was primarily that of conserving and enhancing his estate. The petitioners challenge that conclusion, asserting that respondent's activities in connection with conserving and enhancing his estate did not constitute a "trade or business" within the meaning of § 23(a) of the Act.

But as we view the case it is unnecessary for us to pass on that contention and to make the delicate dissection of administrative practice which that would entail. For we are of the opinion that the deductions are not permitted either within the rule of *Burnet* v. *Clark* or *Welch* v. *Helvering, supra*, even though we were to assume that the activities of respondent constituted a business, as found by the District Court.

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stock. This offer was accepted by the executives. Respondent when he proposed it, stated that he did so "as a large stockholder, and, perhaps, the one to be most benefited by the recovery in value of the Company's shares." He also stated that he wanted the executives to be "free of worry over the unexpected outcome" of the stock purchase plan.

[6] Due to stock dividends and split-ups respondent was obligated to return to Christiana Securities Company 142,212 shares to replace the 9,000 shares which he had borrowed.

[7] Respondent was not a stockholder of the Delaware Company, although it appears that his brother was one of its executive officers.

There is no intimation in the record that the transactions whereby the stock was borrowed were not in good faith or were entered into for any reason except a *bona fide* business purpose. Nor is there any suggestion that the transactions were cast in that form for purposes of tax avoidance. And it is true that as respects the dividends received by respondent and paid over to the Delaware Company, he was little more than a conduit. But allowance of deductions from gross income does not turn on general equitable considerations. It "depends upon legislative grace; and only as there is clear provision therefor can any particular deduction be allowed." *New Colonial Ice Co., Inc.* v. *Helvering*, 292 U. S. 435, 440. And when it comes to construction of the statutory provision under which the deduction is sought, the general rule that "popular or received import of words furnishes the general rule for the interpretation of public laws," *Maillard* v. *Lawrence*, 16 How. 251, 261, is applicable.

By those standards the claimed deduction falls for two reasons. In the first place, the payments in question do not meet the test enunciated in *Kornhauser* v. *United States*, 276 U. S. 145, since they proximately result not from the taxpayer's business but from the business of the du Pont Company. The original transactions had their origin in an effort by that company to increase the efficiency of its management by selling its stock to certain of its key executives. The respondent undertook to furnish the necessary stock only after the company had been advised that it could not legally do so. In that posture of the case these payments are no more deductible than were the payments made by the stockholder in *Burnet* v. *Clark*, *supra*, as a result of his endorsements of the obligations of his corporation. Those payments were disallowed as deductions from his gross income though they arose out of transactions which were intended to preserve his investment in the corporation. Similar payments were disallowed in *Dalton* v. *Bowers*, 287 U. S. 404. Hence, the fact that the transaction out of which the carrying charges here in question arose might benefit respondent does not bring it within the ambit of his alleged business of conserving and enhancing his estate. The well established decisions of this Court do not permit any such blending of the corporation's business with the business of its stockholders. Accordingly, the payments made under the 1919 agreement would certainly not be

deductible. And the fact that a new and different arrangement was made in 1929 with the Delaware Company does not alter the conclusion, for it is the origin of the liability out of which the expense accrues which is material. Otherwise carrying charges on any short sale whether or not related to the business of the taxpayer would be allowable as deductible expenses. That cannot be if the notion of proximate result implicit in the statutory words "expenses paid or incurred . . . in carrying on any trade or business" is to have any vitality.

In the second place, these payments were not "ordinary" ones for the conduct of the kind of business in which, we assume *arguendo*, respondent was engaged. The District Court held that they were "beyond the norm of general and accepted business practice" and were in fact "so extraordinary as to occur in the lives of ordinary business men not at all" and in the life of the respondent "but once."[8] Certainly there are no norms of conduct to which we have been referred or of which we are cognizant which would bring these payments within the meaning of ordinary expenses for conserving and enhancing an estate. We do not doubt the correctness of the District Court's finding that respondent embarked on this program to the end that his beneficial stock ownership in the du Pont Company might be conserved and enhanced. But that does not make the cost to him an "ordinary" expense within the meaning of the Act. Ordinary has the connotation of normal, usual, or customary. To be sure, an expense may be ordinary though it happen but once in the taxpayer's lifetime. Cf. *Kornhauser* v. *United States*, *supra*. Yet the transaction which gives rise to it must be of common or frequent occurrence in the type of business involved. *Welch* v. *Helvering*, *supra*, 114. Hence, the fact that a particular expense would be an ordinary or common one in the course of one business and so deductible under § 23(a) does not necessarily make it such in connection with another business. Thus, it has been held that one who was an active trader in securities might take as deductions carrying charges on short sales since selling short was common in that business.[9] But the

[8] 22 F. Supp. 589, 597.

[9] Dart v. Commissioner, 74 F. (2d) 845. Cf. Terbell v. Commissioner, 29 B. T. A. 44, aff'd. 71 F. (2d) 1017, where such carrying charges were disallowed as deductions. The Board of Tax Appeals said, p. 45, "We have only the stipulated facts and there is no suggestion in those facts that the decedent was engaged in the business of making short sales or in dealing in securities generally."

carrying charges on respondent's short sale in this case cannot be accorded the same privilege under § 23(a). The record does not show that respondent was in the business of trading in securities. Nor does it show that a stockholder engaged in conserving and enhancing his estate ordinarily makes short sales or similarly assists his corporation in financing stock purchase plans for the benefit of its executives. As stated in *Welch* v. *Helvering, supra,* pp. 113-114: " . . . What is ordinary, though there must always be a strain of constancy within it, is none the less a variable affected by time and place and circumstance." One of the extremely relevant circumstances is the nature and scope of the particular business out of which the expense in question accrued. The fact that an obligation to pay has arisen is not sufficient. It is the kind of transaction out of which the obligation arose and its normalcy in the particular business which are crucial and controlling.

Review of the many decided cases is of little aid since each turns on its special facts. But the principle is clear. And on application of that principle to these facts, it seems evident that the payments in question cannot be placed in the category of those items of expense which a conservator of an estate, a custodian of a portfolio, a supervisor of a group of investments, a manager of wide financial and business interests, or a substantial stockholder in a corporation engaged in conserving and enhancing his estate would ordinarily incur. We cannot assume that they are embraced within the normal overhead or operating costs of such activities. There is no evidence that stockholders or investors, in furtherance of enhancing and conserving their estates, ordinarily or frequently lend such assistance to employee stock purchase plans of their corporations. And in absence of such evidence there is no basis for an assumption, in experience or common knowledge, that these payments are to be placed in the same category as typically ordinary expenses of such activities, e. g., rental of safe deposit boxes, cost of investment counsel or of investment services, salaries of secretaries and the like. Rather these payments seem to us to represent most extraordinary expenses for that type of activity. Therefore, the claim for deduction falls, as did the claim of an officer of a corporation who paid its debts to strengthen his own standing and credit. *Welch* v. *Helvering, supra.* And the fact that the payments might have been necessary in the sense that consummation of the transaction with the Delaware Company was beneficial to respondent's estate is of no aid. For Congress has not de-

creed that all necessary expenses may be deducted. Though plainly necessary they cannot be allowed unless they are also ordinary. *Welch* v. *Helvering, supra.*

We conclude then on this phase of the case that as the District Court, on a correct interpretation of the Act, found that these payments did not proximately result from, and were not ordinary expenses for the conduct of, respondent's alleged business, it was error for the Circuit Court of Appeals to reverse the judgment for petitioners. *McCaughn* v. *Real Estate Land Title & Trust Co.*, 297 U. S. 606.

There remains respondent's contention that these payments are deductible under § 23(b) as "interest paid or accrued . . . on indebtedness." Clearly respondent owed an obligation to the Delaware Company. But although an indebtedness is an obligation, an obligation is not necessarily an "indebtedness" within the meaning of § 23(b). Nor are all carrying charges "interest". In *Old Colony Railroad Co.* v. *Commissioner*, 284 U. S. 552, this Court had before it the meaning of the word "interest" as used in the comparable provision of the 1921 Act (42 Stat. 227). It said, p. 560, " . . . as respects 'interest', the usual import of the term is the amount which one has contracted to pay for the use of borrowed money." It there rejected the contention that it meant "effective interest" within the theory of accounting or that "Congress used the word having in mind any concept other than the usual, ordinary and everyday meaning of the term." p. 561. It refused to assume that the Congress used the term with reference to "some esoteric concept derived from subtle and theoretic analysis." p. 561.

We likewise refuse to make that assumption here. It is not enough, as urged by respondent, that "interest" or "indebtedness" in their original classical context may have permitted this broader meaning.[10] We are dealing with the context of a revenue act and words which have today a well-known meaning. In the business world "interest on indebtedness" means compensation for the use or forbearance of money.[11] In absence of clear evidence to the con-

[10] Respondent refers to the *mutuum* in Roman Law. Ledlie's Sohm's Institutes of Roman Law (2d. Ed.), p. 395; Hare, The Law of Contracts, p. 73.

[11] This makes irrelevant other lines of authority cited by respondent where "interest" in a different context has been used to describe damages or compensation for the detention or use of money or of property. See United States v. North Carolina, 136 U. S. 211, 216; N. Y. General Business Law, § 370, which provides, "The rate of interest upon the loan or forbearance of any money, goods, or things, in action . . . shall be six dollars upon one hundred dollars, for one year, . . ."

trary, we assume that Congress has used these words in that sense. In sum, we cannot sacrifice the "plain, obvious and rational meaning" of the statute even for "the exigency of a hard case." See *Lynch* v. *Alworth-Stephens Co.*, 267 U. S. 364, 370.

Petitioners throughout have referred to these payments by respondent as being capital in nature. Cf. *Bonwit Teller & Co.* v. *Commissioner*, 53 F. (2d) 381; *Hutton* v. *Commissioner*, 39 F. (2d) 459; *Bing* v. *Helvering*, 76 F. (2d) 941. What appropriate treatment may be accorded these items of cost under other provisions of the Act we do not undertake to say, as that issue is not here.

The judgment of the Circuit Court of Appeals is reversed and that of the District Court is affirmed.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 151.—October Term, 1939.

Pearl E. Deputy, and the Sussex Trust Co., a Corporation of the State of Delaware, as Administratrix and Administrator of the Estate of Willard P. Deputy, Deceased, Late Collector of Internal Revenue, Petitioner,
vs.
Pierre du Pont.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[January 8, 1940.]

Mr. Justice Frankfurter, concurring.

What the activities of a tax payer are is an issue for determination by triers of fact. Whether such activities constitute a "trade or business" as conceived by § 23(a) of the Revenue Act of 1928 (45 Stat. 791, 799), is open for determination here unfettered by findings and rulings below except for the weight of the intrinsic authority of all lower court opinions. To avail of the deductions allowed by § 23(a), it is not enough to incur expenses in the active concern over one's own financial interest. " . . . carrying on any trade or business", within the contemplation of § 23(a), involves holding one's self out to others as engaged in the selling of goods or services. This the taxpayer did not do. Expenses for transactions not connected with trade or business, such as an expense for handling personal investments, are not deductible. It is otherwise with losses. § 23(e)(2). Without elaborating the reasons for this construction and not unmindful of opposing considerations, including appropriate regard for administrative practice, I prefer to make the conclusion explicit instead of making the hypothetical, litigation-breeding assumption that this tax payer's activities, for which expenses were sought to be deducted, did constitute a "trade or business".

Mr. Justice Reed joins in these views.

SUPREME COURT OF THE UNITED STATES.

No. 151.—October Term, 1939.

Pearl E. Deputy and The Sussex Trust Company, etc., Petitioners, vs. Pierre S. duPont. } On Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

[January 8, 1940.]

Mr. Justice Roberts.

I feel constrained to state my views, not because this case raises any important issue of law which should be settled by this court; but, on the contrary, because I think it presents a question the answer to which depends solely upon the facts disclosed by the record. Decision of the controversy cannot be helpful in the administration of the Revenue Acts or set any important precedent. I think the writ should not have been granted and that it now should be dismissed as improvidently granted. The amount of taxes involved or the insistence of the Government that the court below erred in its application of the law to the facts are not adequate reasons for review. There is no dispute as to principle and no conflict with any case in the application of any principle.

The function of this court is to resolve conflicts of decision and to settle important principles of law. The discretionary power of this court to review judgments of lower federal courts was not intended to be exercised in every case where those courts have adjudicated the conflicting claims of the parties, which involves no important principle of law and no conflict of decision amongst the federal courts. Our rules adopted to carry out the policy of the statutes granting the power to bring cases here by certiorari have apprised the Bar and the public that we will not take cases fully heard and adjudicated below for the mere purpose of reexamining the correctness of the result. (See Rule 38, par. 5.)

The dominant purpose evidenced by the income tax statutes is to tax net income. The policy is to credit against gross income the expenses of the business which begets earnings. The taxpayer is entitled to deduct that which he reasonably and in good faith ex-

pended in the effort to realize a profit. The revenue acts have always characterized deductible expenses as the ordinary and necessary expenses of the business, incurred and paid during the taxable year. The opinion assumes that the expenditure here in question was necessary in the conduct of the taxpayer's business but holds that it was not an ordinary expense of that business. Obviously what is an ordinary expense of a given business must depend upon the nature and scope of the business, the nature and occasion of the expenditure, and other considerations which will emerge in each specific case. Necessarily the decision of one case will have slight, if any, bearing upon the proper decision of another. If this court is to take under review every dispute in which the Government and a taxpayer differ as to whether a given expenditure is an ordinary or an extraordinary expense of the taxpayer's business we shall be involved in the decision of myriad cases, each turning upon its own facts, without furnishing any light to the taxpayers for their future guidance. I think this is the result of the court's opinion. It is admitted that the fact that the expenditure occurred but once in the taxpayer's experience does not render it extraordinary. It must be admitted that the fact that it is a large transaction does not render it extraordinary. What the opinion does, in the upshot, is to canvass all the circumstances and reach, as I think, a conclusion based solely upon the peculiar facts of this single case. We have repeatedly warned the Bar and the public that this we will not do because we do not sit for any such purpose.

An added reason for refusing to decide the case is the admission that the Treasury and the Board of Tax Appeals in years past have held a similar expense incurred in earlier years an expense of the taxpayer's business. In a matter resting so much in judgment and discretion as the determination of what is ordinary and what extraordinary expenditure in a business the weight of a continued administrative construction is of peculiar importance; and we ought not now depart from the rule long observed that such practice is entitled to high consideration at the hands of the courts and should not be overturned unless clearly wrong and for the most cogent reasons.

Since the case has been taken and considered on the merits I think the judgment below should be affirmed. I need add little to the opinion of Judge Maris of the Circuit Court of Appeals, with

which I agree. The taxpayer borrowed stock in order to sell it for cash to others. His contract obligated him either to return the stock or to pay the carrying charges to the lender. What he paid was not technically interest but it was an expense necessary to his obtaining and using the stock. He had several alternatives: to pay the annual carrying charges, or to default, and, in that case, to go into the market to buy the stock and return it to the lender or to pay the lender the value thereof.

What was there extraordinary about this transaction as compared with the borrowing of any commodity other than stock for a business reason and with a business purpose? In the conduct of every business situations arise which must be met. The circumstance that such a situation had not theretofore arisen, or that the transaction was the first of its kind in the respondent's business experience, does not render it extraordinary in the sense in which the statute uses the term. The limitation placed by Congress upon the types of expenditures made deductible was intended to prevent evasion of payment of tax on true net income, which confessedly was not a motive in the present instance. I think that under the guise of enforcing the plain mandate of the statute the court is really reading into the law what is not there and what Congress did not intend to place there.

To suggest, even by indirection, that perchance the taxpayer's expenditure may be treated as a capital expenditure is, in my judgment, to keep the word of promise to the ear and break it to the hope. In my view the carrying charge of the taxpayer's loan was either an ordinary expense of his business or it was nothing of consequence under any provision of the statute.

Mr. Justice McReynolds joins in this opinion.